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TRANSCRIPT OF PROCEEDINGS

PRODUCTIVITY COMMISSION

INQUIRY INTO POST 2005 ASSISTANCE ARRANGEMENTS FOR THE AUTOMOTIVE MANUFACTURING SECTOR

MR G. BANKS, Chairman
MR P. WEICKHARDT, Associate Commissioner

TRANSCRIPT OF PROCEEDINGS

AT ADELAIDE ON THURSDAY, 25 JULY 2002, AT 8.59 AM

MR BANKS: Good morning, ladies and gentlemen. Welcome to the first day of the public hearings for the Productivity Commission's Inquiry Into Post 2005 Assistance Arrangements for the Automotive Industry. My name is Gary Banks. I'm chairman of the Productivity Commission. On my left is Philip Weickhardt, who's associate commissioner for this inquiry.

The purpose of these hearings is to provide those who have an interest in the inquiry with the opportunity to present submissions in response to the commission's position paper, which was released about four weeks ago. As you know, we chose the position paper format rather than a more comprehensive and detailed draft report because of timing considerations, but we're sure to focus in that position paper on the key considerations that would be informing our findings to give you the opportunity to comment on those.

After these hearings in Adelaide, we're going to have three days in Melbourne from Monday next week. We'll then proceed to prepare our final report. We're aiming to complete that report by the end of August, rather than the due date of 21 September, in light of the government's own time frame for making a decision on these issues.

The public hearings, we find, have a useful role in allowing anyone to have a say in person on the issues under consideration and for others to listen to those remarks and respond, if they wish. If anyone wants to appear at the hearings, having heard what others have said, they should approach the staff and we'll make room for them to do so. The hearings are as informal as possible, but the act does require that people be truthful in their remarks, and a transcript is made of the proceedings, which we endeavour to place promptly on the commission's web site. I think it typically takes a few days to have that transcript prepared and put on the web site.

I would remind participants that all submissions really need to be in by early August - I think about 2 August is the date we've got in mind - just to allow us to draw on them adequately in working through our final report, which has to be completed by the end of the month.

I should also take this opportunity to thank those participants who have assisted us so far in this inquiry. We've had a lot of cooperation, we've had some excellent submissions and it's made our job a lot easier. We're now looking forward to the next phase and the next set of reactions to our position paper to help us complete the final. With those introductory remarks over, I'd now like to welcome the Federated Chamber of Automotive Industries and ask its representatives to give their names, please, and their positions.

MR STURROCK: Thank you, Mr Chairman. I'm Peter Sturrock, the chief executive of the Federal Chamber of Automotive Industries.

MR McKELLAR: I'm Andrew McKellar, executive officer of FCAI.

MR BANKS: Good, thank you. Thank you for attending today and being first. As I said, it's always good to have the peak organisations appear at the start of the hearings. You've provided a preliminary submission in response to our position paper and also a first quite comprehensive submission and we might have a couple of questions to put to you on that as well. As we discussed, I'll give you the opportunity now to perhaps summarise the key points that you'd like to make.

MR STURROCK: Thank you, Mr Chairman. Good morning everybody. The Federal Chamber of Automotive Industries welcomes the commission's position paper as a very constructive contribution to the consideration of policy options to apply to the Australian automotive industry after 2005. In particular, we welcome the commission's acknowledgment of the industry's desire to establish a clear policy path providing greater certainty over a period of at least five years and preferably 10 years beyond 2005.

It is worth noting that the chamber accepts the goal that assistance arrangements for the Australian automotive industry should ultimately move into alignment with other manufacturing industries. However, the chamber believes achievement of this objective needs to be balanced against at the least the following two considerations: firstly, the competing policy environment affecting decisions about the location of international automotive investment in other competing markets, particularly within the Asia-Pacific region and, secondly, the adjustment costs associated with the transition to a lower assistance environment. In particular, we are pleased to note that the commission, in considering appropriate policy options for the industry after 2005, has sought to ensure that the industry will have time to adjust to the prospect of future changes in the policy environment.

Turning to the various issues, tariff: each of the options for future tariff policy advocated by the commission in its position paper involves the establishment of a predetermined timetable for reduction in tariffs on motor vehicles and automotive products to a target of 5 per cent over the period to either 2010 or 2015. However, the chamber is concerned that Australia should not prematurely agree to further concessions that may undermine our competitiveness as an investment location without further testing the scope for meaningful progress on trade and investment issues.

Under current policy settings, Australia's vehicle market and automotive industry are characterised by significant levels of international investment, an internationally high level of import activity, a wide diversity of available brands and models and very competitive levels of vehicle affordability. The chamber therefore urges the commission to consider the inclusion of an additional tariff option that would see automotive tariffs maintained at 10 per cent beyond 2005.

While not demurring from the ultimate objective of aligning automotive tariffs with that of other manufacturing industries, it would be open to the Australian government to consider future reductions in automotive tariffs below 10 per cent in the context of a range of possible future developments, including the following: firstly, progress in reducing barriers to trade in industrial products in the forthcoming WTO round; secondly, progress toward implementation of the APEC goals of free and open trade and investment through the Asia-Pacific region; thirdly, Australian involvement in regional free-trade agreements, including the development of a future agreement with AFTA; fourthly, implementation of future bilateral free-trade agreements, including possible agreements currently being considered with Thailand and the United States; finally, but most importantly, Australia's competitive standing as a location for international automotive investment.

Specifically now turning to ACIS: ACIS was instigated with the intention of providing a competitive incentive for renewed and additional international investment in the Australian industry. This scheme also incorporates the duty-free allowance - or the DFA - which the government agreed to continue in 1997. The DFA, now delivered in the form of uncapped ACIS productions, is designed to partially offset the impact of tariff assistance for domestic component producers on the input costs of vehicle manufacturers. The chamber believes that, consistent with the government's earlier decision, the DFA should continue uncapped and be treated as a separate and distinct issue to evaluation of the appropriate quantum of funding and design of the $2 billion capped elements of ACIS.

The chamber has undertaken some preliminary projections of the cost of a renewed ACIS scheme over the period 2006 to 2010. On the basis of these projections, the level of demand credits in a renewed ACIS would again exceed $2 billion by a significant margin. It is our view that renewal of the currently capped elements of ACIS with funding of at least $2 billion over the five-year period 2006 to 2010 would be the minimum position supported by the industry.

The commission's position paper acknowledges that there is a case for establishing separate funding pools for ACIS, for vehicle producers and component manufacturers within a renewed ACIS. One issue of contention for vehicle manufacturers associated with the operation of ACIS in its current form has been the impact of stronger than expected growth in demand for credits from the ACP participants. Most recent estimates project that MVP participants will receive ACIS credits worth around $991 million or approximately 49 per cent of available funding. Whilst all other categories will receive $1.009 billion, or around 51 per cent, this represents a significant and material deviation from the initial expectations of motor vehicle producers, and from the notional allocations indicated by the then ministers Fischer and Moore.

The chamber submits that the determination of the appropriate split between separate funding pools should be determined by way of agreement between industry and the government, once an in-principle decision on the quantum of funding and the time profile for a renewed scheme have been finalised. The chamber has also suggested that considerations could be given to ways of enhancing support for R and D innovation and investment in the industry. We retain an open mind on the introduction of appropriate modifications to ACIS to support these objectives.

Turning now to industrial relations issues. The chamber welcomes the commission's observations about the substantial progress that has been made over the last decade or so to improve the flexibility and the productiveness of the automotive workplaces. Nonetheless, we acknowledge that significant issues remain to be addressed to bring some Australian workplaces up to world-best levels. The chamber reiterates its support for current proposed legislative amendments to strengthen the integrity of genuine bargaining arrangements and the introduction of secret ballots to help reduce the risk of unnecessary and illegitimate industrial action.

We also believe consideration should be given to further amendments to provide increased protection against disputes that cause significant disruption to third parties within the industry, and to increase penalties for noncompliance with court decisions. To this end we have supported a proposal that will allow the Industrial Relations Commission to implement cooling-off periods, suspending protected industrial action to allow for mediation of a dispute, and to terminate the right to take industrial action where significant damage is likely to be caused to innocent third parties.

Turning now to taxation policy. We welcome the commission's assertion that the luxury car tax has a number of deficiencies and that there may be a case for abolishing this tax. The chamber supports the commission's assessment that, at the very least, there are grounds for raising the threshold above which the luxury car tax applies. We reiterate our support for the eventual abolition of the luxury car tax. As indicated in our initial submission, the chamber believes there is an immediate measure - that the threshold for tax should be increased to restore earlier relativities with significant pricing points, in the Australian vehicle market. On this basis the chamber believes it would be necessary to increase the threshold from its current level of $57,009, to around $78,000.

On matters of safety and environmental issues, the chamber welcomes the commission's observation about the importance of consultation with the automotive industry in the setting of future fuel consumption targets, and the need for policy-makers to take account of all of the costs of more stringent targets. The chamber does not accept the assertion made by the Australian Greenhouse Office in its submission that achievement of the government's stated target of a 15 per cent improvement in average fuel consumption over business as usual by 2010 translates into an objective of 6.3 litres per 100 kilometres.

As noted by the commission, the industry has proposed a cooperative target of 6.8 litres per 100 kilometres by 2010. This proposal remains open for further discussion between industry and the government, and the chamber is hopeful that these negotiations will be completed in coming months. Mr Chairman, that concludes the chamber's comments at this morning's hearing. Again, thank you for the opportunity to present them to you here.

MR BANKS: Thank you very much for that. You have raised a number of points that we might just explore a little bit more. I think the first one that I thought might be useful to talk about relates to the question of the tariff - the future of the tariff, and to what extent that should be contingent on other things, what other countries might do, and so on. On page 11 of your submission, and again in your remarks, you have not demurred from the ultimate objective of aligning our tariffs with those for other manufacturing industries, but you have talked about considering future reductions in the context of a range of possible future developments, and you have given a number and you went through those today. I guess, as we try to think about what that means, we would appreciate any comments from you as to, operationally, how you would see that being achieved, this kind of linkage with what other countries are doing, and the other things that you have raised.

MR STURROCK: I think the key point is that we don't see that there should automatically be a definitive reduction in tariff at a particular year without consideration of the climate, the international climate, and the industry issues at that time. They particularly relate to the investment movements, the structure of the industry, and the trade issues with our immediate partners; trade, in the sense of the opportunities for further advancement of trade liberalisation, the status of those aspects, the issues with AFTA, and potentially where Australia stands in relation to its activities on bilateral free-trade agreements with countries such as Thailand and the USA. There are a number of those factors that we think are very important, and we think that there needs to be due consideration given to those matters in a wider sense before there should be a particular reduction further in the tariff.

MR BANKS: I guess what I wanted to explore a little bit further was just how that due consideration would occur. Would it be simply the government monitoring these things and at some point deciding that the balance had shifted, or would there be a standing review, or are you implying there should be another review, such as this, that would look into those matters?

MR STURROCK: We are not advocating that there should be specifically another review per se. What we are saying is that there needs to be, and there would be obviously, close consultation between the industry and government right through the period - let us assume that is to the end of the decade. As the industry continues to grow and advance, much of the objectives have been established, and I would have thought that there would be the mechanism within those direct dialogues between industry and government to consider what is appropriate at that time, and what we are not saying is necessarily we need to put anything formally in place beyond that monitoring process, that dialogue between industry and government.

MR BANKS: Doesn't that conflict with the industry's desire also for some greater certainty about future assistance arrangements, and to have that information now, to allow planning for investment and so on?

MR STURROCK: I don't think so, in the sense that we have sought - as has been put in our submission - the fact that the tariff remain at 10 per cent right through to the end of the decade as a minimum period. That is effectively seven or eight years from now. Secondly, we have sought the renewal of the ACIS scheme in broadly its current structure, with some potential minor modifications to the administration of the scheme. But fundamentally, those two planks, together with the determination on industrial relations, together with the determination on the trade and access to markets and so on, remain the key issues for the industry. That provides us for a period right through to 2010.

We are suggesting that, as part of the long-term strategy for the industry, to take it through to 2015 would be most appropriate. I don't think, therefore, what we are suggesting by way of a tariff position is inconsistent with that. We have the fundamental issues confirmed should the plans be established in that fashion, and I think that that would be a very adequate position for the industry to work towards.

MR McKELLAR: If I can just add a point to that, Mr Chairman. I think the position we have articulated in the submission with regard to that issue is consistent with the policy that the government has adopted in its response to the earlier review of general tariff arrangements where, in essence, it has signalled that it maintains the current level but will review it periodically and look at developments in the context of trade liberalisation more broadly and market access for Australian products and, at an appropriate time, it may be contemplated that certain tariff lines could be further reduced and so on, and it will look at the circumstances when that might appropriately occur.

So the issue of certainty for the industry, I think, is provided by the conditions that the industry has signalled in the submission here that would need to be met before there is a further reduction and, in particular, having regard to the competitive environment globally, Australia's position in that respect for investment in the industry in this country and, provided those conditions are met, then there isn't an obstacle for future reform because the industry would have certainty rather than providing or setting a predetermined timetable that doesn't take account of changes that would be occurring elsewhere in the region in other countries in terms of their policies. I guess that is the position we have tried to articulate.

MR BANKS: I just make the observation that the transparency of such an approach would be somewhat diminished, I think, relative to what we are going through now because you're not really asking for any kind of public review at that time but, rather, a matter of negotiation between the industry and the government to decide if and when the time was right. I would suggest to you that perhaps the time would never be right in the circumstances, but clearly there would be others who would see themselves having a view about those matters, who would be excluded from such a process.

MR STURROCK: At the end of the day it is the industry working closely with government in terms of the appropriate structure of policy setting, negotiating those settings with government and, as we have highlighted on various occasions, the key to all of this is the additional and continuing investment in Australia in manufacturing to sustain the viability of manufacturing in this country. The policy settings are fundamental to that and the circumstances of our trading partners and other locations around the world are fundamental to that in attracting investment and maintaining the industry's growth. So we have to ensure that with our policy settings we are internationally competitive, that we do have the right environment to continue to encourage the shareholders of these corporations who fundamentally have a very significant stake in this process, decision-making process, to continue that investment, to maintain that growth, and therefore to deliver on the strategy that the industry has identified.

MR WEICKHARDT: I would be grateful if you could just help me to understand a bit more some of the comments you've made in relation to this issue of negotiating coin, which you raise as a reason why the government should not at this stage - prematurely in your view - reduce tariffs further. You raise on page 8 of your submission some comments about the Howe Leather case as an example of the practical demonstration of negotiating coin. I'm afraid I didn't really understand that issue, but if I could just go on further than that and say that you then, I think, on the following page refer to the fact that the ASEAN business leaders have said, "Well, since the tariff is already so low, so there is no negotiating coin" - which is an argument I've heard - and then you go on further and talk about the fact that negotiating coin is really around bound rates, which I suspect is the case, so I'm left confused really as to what the issue is that you're trying to drive at there.

MR STURROCK: Let me ask Andrew to comment on that issue. The Howe Leather case is a specific issue which was the subject of some concern as it was to seek a resolution, and the other matters are significant, so let me ask Andrew to comment on that.

MR McKELLAR: I guess in particular what we were referring to in that situation is that the - I guess we have seen on a number of occasions the trade minister Mark Vaile make public reference to the fact that he believes that Australia can use, even at reasonably minimal levels, some of its remaining tariff rates as potential negotiating coin in arriving at particular trade outcomes. We cited the Howe Leather case as a potential example of that. It's a fairly specific example where the Australian government, in the interests of resolving a trade dispute with the United States, agreed to a number of steps, including the removal of tariffs on a number of items - I think there was a total of about 30 items, all up.

So there was a case where the government was able to identify some trade liberalising measures that it could take and use that in achieving an outcome and resolving a trade issue, and resolving it in a way which served the national interest and served the Australian commercial interests. I guess we picked on that as a particular example of a case where Australia may have some leverage to achieve outcomes through liberalising measures.

MR WEICKHARDT: Can I just clarify? Was that liberalisation of bound rates?

MR McKELLAR: I would have to refer back to the agreement. I believe it was. I believe the agreement was that the bound rates would be taken to zero in those cases.

MR BANKS: Just further to that, I imagine that the Americans' main concern. however, was to what extent what they perceived to be an export subsidy was removed - in other words, what impact this settlement had on what they saw as subsidised exports to the USA.

MR McKELLAR: Sure. There was that broader issue. I guess what we are pointing to is the fact that within the terms of the settlement of that agreement though, there was a position arrived at where Australian industry agreed that some tariff lines could be addressed and became part of the settlement - was part of the negotiating coin that the Australian government was able to use in that context to resolve a dispute with the United States and achieve an outcome that was mutually beneficial.

MR WEICKHARDT: I guess my confusion arises from the fact that these arguments are often put along the lines there is negotiating coin and yet if it's around bound rates, well, nothing you do with the actual rate removes that negotiating coin. If it's around actual rates I think most of the modelling suggests that the effect on any other economy of us reducing our actual rates further is infinitesimal. The modelling work, from memory, suggested that Korea's GDP would go up by .001 per cent or something. I can't imagine they're going to give away a lot for that.

MR McKELLAR: No. I think the issue of bound and actual rates is a germane issue obviously in the current context. I don't think anyone would claim that we had a huge leverage in terms of remaining applied rates, and I think that is borne out by the sort of statement, or the reflection, that comes back in the context of the CER-AFTA negotiations and the lack of leverage that we potentially had there. I think the Howe Leather case illustrates that in some specific instances there is limited scope to utilise that leverage there. I guess what we're saying is that, even at these low levels of applied rates, one should not necessarily prematurely move to reduce those rates further without first looking at Australia's overall competitive position as an investment location, and that is still a variable that international shareholders in the industry look at when they are assessing Australia as a location for global investment.

I think that's the fundamental point we have to keep coming back to - that it is not just a domestic argument. It's not a case of looking at what is the level of tariffs on automotive products versus general manufacturing. It is what is the level of automotive tariffs internationally and what are those international shareholders looking at when they are making decisions about future investment in Australia. I guess that is the crux of the argument that we really have to keep coming back to - that we have to look at this in a global context and see it from the perspective of those international shareholders. I think that is at the heart of the argument that we are presenting in the submission.

MR BANKS: But I guess you would agree that you would need to make both international and domestic comparisons.

MR McKELLAR: Mm.

MR BANKS: There may in future be an inquiry into the TCF industry and I am sure they, too, will argue that TCF is very highly protected in other countries and that's the benchmark for us, so clearly that is not the only thing that government can think about. Do you agree with that?

MR STURROCK: I think so. We have a very open market with the reform that has been implemented in the last 10 to 15 years. We have now a manufacturing domestic market that is 30, 35 per cent of the vehicle market. The import sector dominates the market. That's quite unusual by international comparisons. It's the reason why it is essential for the continuing encouragement of ongoing investment, the drive towards the internationally competitive structure of our industry in relation to other parts of the world, and why it is so essential that the policy settings need to maintain that encouragement for investment, maintain the drive, innovation R and D, technology improvements and continually lift the bar in terms of efficiency and quality so that we can compete and can remain a viable manufacturing sector within the international arena. It is a very tough challenge. It is a very difficult task. The industry has been extremely pleased with the progress it has been able to make in that environment under the existing policy settings that were confirmed back in 1997, and hence our very keen wish for those fundamentals to be maintained for this next period.

MR WEICKHARDT: I guess arguably, Peter, you could say the government also has a role to try and make the economy as attractive a location for investment as it can.

MR STURROCK: Certainly.

MR WEICKHARDT: Get taxes down, micro-economic reform, keep skills and education up, and those are issues that also affect the attractiveness of the location for investment. Do you agree with that?

MR STURROCK: Yes, absolutely, and we've been praiseworthy of the government in terms of its economic reform - the progress, matters such as taxation reform, GST and so on, the way that has assisted in this process - and there is no question that those fundamentals are essential to ensure that there can be economic stability, there can be growth and that that can assist in the process of encouraging our shareholders to continue to invest in this country.

MR WEICKHARDT: Good. Thank you. You make some comments in relation to APEC, for which we're grateful, in this response to our position paper. You talk about, as yet, other developed countries not having provided a firm indication of their timetable. I guess there's a bit of a catch-22 here in a sense, in that, as I was indicating earlier, Australia is having this review because of the need to chart a course for the industry in policy terms, and in a sense what you're saying is that having it now means that we are making a decision before other countries. So it's sort of in some ways the flip side of what you've asked for in terms of getting some certainty about the regime earlier rather than later. I don't know whether you'd like to respond to that or not. But we do have the Bogor statement which, in broad terms, is a commitment. What you're saying is, they haven't put the flesh on those bones, in a sense, in terms of very fixed schedules of reduction.

MR STURROCK: I think it comes back to the basic issue of long-term planning and the nature of the cycle of this industry, where we're dealing with five, seven, 10 years in terms of investment decisions, technology improvements, model developments and significant investment having to be made in accord with those plans. As best we would like to see it, we have always believed that it is better to have a longer-term view in terms of policy and issues, as best it can be described in detail, in order that the industry can be aware of those circumstances, can plan effectively and can continue to seek support from their shareholders. That is the fundamental issue in the first place.

In second place, in terms of APEC and the other trading issues is that, as has been reported from time to time, Australia has been frustrated in terms of some of the other APEC economies committing to firm plans in terms of market liberalisation and tariff reduction. There has been some progress but it is quite slow. Nevertheless, we believe it is essential that the government maintains its commitment to the APEC process to encourage the other economies to liberalise, to adopt more realistic policies going forward, again over a long time frame, because ultimately that is the only gain that is going to be productive for us as a country in our region.

Again, we are all aware of the small-sized market and our geographic location in relation to some of our APEC trading partners. That won't change, relatively speaking, but I think we can continue to work cooperatively and effectively in those trade fora in trying to seek progress and trying to secure commitments from trading partners and trying to ensure that there can be trade liberalisation over time. It is no easy task, and that's been commented on regularly by government ministers, but we still see it to be a very important task nevertheless.

MR WEICKHARDT: If we think about the genesis of APEC and so on, clearly Australia played an initiating role, and I guess what you're saying is that if APEC came true, from Australia's point of view that would be a very good thing in terms of the Bogor commitments being met in our export markets. I'd just get you to reflect on whether you think a signal by Australia that it was going to wait and see what other countries did before it really revealed its own hand in terms of those commitments might impact on the dynamic of the rest of the region and what they might do as well; in other words, could that be a counterproductive strategy in terms of our bigger goal, which is to ensure that other countries also meet their APEC commitments?

MR STURROCK: I think hypothetically if we were to have a situation occur where our tariff levels on passenger vehicles fall to 10 per cent in 2005 and if they were to remain thus at least until 2010, at that level it is a very low level of assistance or protection. It is at the lower end of the scale, particularly in relation to a 5 per cent general tariff position, and we would believe that that could be quite simply justified in government negotiations country to country in terms of a relatively free and open market, a relatively advanced international trading structure, and one that I think the government could be comfortable in adopting.

As I said at the outset of that remark, that hypothetical issue is one that I think could be sustained, but it is an example of that position, and I don't think that that necessarily exposes Australia to any uncertainty in terms of future tariff settings. I think at a 10 per cent level, it is a very low level indeed, particularly in relation to our immediate APEC trading partners.

MR WEICKHARDT: How in broad terms would you value the ACIS package relative to the assistance provided through the tariff, say at 10 per cent?

MR STURROCK: The ACIS support has been fundamental in the ongoing encouragement of further investment, particularly the drive towards research and development, new technologies and innovation. It is the future of the industry in manufacturing in this country. The industry recognises that it has potentially a role of manufacturing in this country for other world markets but, to do so, it has to continually innovate and provide products which can be sold in niche or small volumes in various markets of the world; small volumes in an Australian sense but into a large market elsewhere in the world. It can be achieved. That is essential, and in that respect the ACIS structure has been, in our view, fundamental to the current growth of the industry, the current investment by many many companies in their Australian subsidiaries or by Australians in their own companies, and we see that as vital and an essential element of the plan going forward.

It is still a transitionary scheme. We are still moving through that transitionary process, and we have made the point very firmly in our submission that that transition continues. We would see that it is an essential element of that transition at least until the end of the decade, 2010, and that, given the other circumstances we have already highlighted - trade arena, the international structure of the industry, other matters which may occur over the next seven or eight years - we do think nonetheless that that is an essential element and is highly valuable to the industry.

MR BANKS: But it seems implicit in what you are saying, while you see it as a transitionary stream, you don't see it being transitional in the sense of being predicated on a further reduction in the tariff.

MR STURROCK: No, I think that the two things run in parallel. We have the ACIS structure as a fundamental structure for the investment and other issues we've already identified, and that is substantial plank. Beside that, the tariff issue, as has been acknowledged, falling to 10 per cent in 2005: we are asking for that to be preserved until 2010. We see that as being an essential element of the encouragement and assistance. It is in the area of the policy setting that those two issues are complementary and need to be very firmly regarded. We believe that it is essential for those to remain so to ensure that the shareholders of our organisations remain interested, committed and positive about the ongoing investment in our industry.

MR WEICKHARDT: Peter, there is a section in your submission that refers to the Deloitte survey commissioned by the FCAI on ACIS and indeed you suggested you intend to make a copy of the final report available to the commission. We would welcome seeing that.

MR STURROCK: Yes, we certainly would like to do that.

MR WEICKHARDT: I'm not sure when that will be available.

MR STURROCK: It can be provided virtually straightaway.

MR McKELLAR: Certainly by 2 August deadline - yes, absolutely.

MR WEICKHARDT: Okay. I guess, as a general sort of question, what I'd be interested in is how this survey has avoided the inevitable risk - if you ask somebody, "What would you have done if you didn't get this money?" most human beings, most children when they're given some pocket money would say, "I would have been even naughtier if you hadn't given me that and, you give me a bit more, I'll be a bit better still." How has that sort of issue and bias potentially been removed from the survey?

MR STURROCK: We had commissioned Deloittes to undertake the study to be as objective as it possibly could be in terms of seeking the views of companies in confidence to those particular questions. Now, I think it's fair to acknowledge that there is a degree of subjectivity and variation in those responses, and I wouldn't disagree that there is some risk of a more positive attitude than a less positive attitude in the survey. Nevertheless, we believed it was an essential task to be undertaken, that we needed to provide the opportunity for companies to identify an A and a B scenario with ACIS support, without ACIS support and the impact it had on their businesses, and then in aggregate to try and take a reading as to the impact that the ACIS support did provide.

I don't think there is any doubt in our minds that it has provided very substantial encouragement and assistance in the process, particularly as it has applied to research and development, productive assets, the R and D issues that we've mentioned earlier and, again, which still remain so critical for the future advancement of the industry. I think that in studying the report you will have the opportunity to see some more of the detail, but fundamentally that was our objective in commissioning the study. That was the spirit with which we entered into it with the various industry players and that was the way in which it was portrayed, and we were seeking, as objective as possible, their input and their comments to the study.

MR McKELLAR: If I could just add to that or reinforce that. It's certainly the case that there is that sort of information in there about what would the case situation be in the absence of ACIS, and it's true that there are those issues presented and those questions were in the study, but I don't think that was the only issue we were looking at. We were trying to use the study, I guess, to provide a guide as to how ACIS was actually affecting the decision-making processes within the firms in the industry, and was it that they were responding simply to the direct subsidies that were provided or the direct incentives that were provided by the scheme? Was it providing an incentive for other sorts of activities and investments to take place, and so on?

So sort of stepping away from the issue of the overall quantum effect - and one can take that at face value or you can ask questions about that quite legitimately - I guess the other objective that we had probably more in mind was the case of how the scheme is actually affecting investment decisions, undertaking particular sorts of activities versus other sorts of activities and, even though these activities are the issue of direct support, does that mean that that's the only result coming out of the scheme or is it having other impacts as well, and I guess we were trying to use the study to try and get behind some of those sorts of issues. As Peter says, we will present the findings of that study to the commission. We've just reported it at face value here and we will leave it to you to determine the merit of the value that that study has in your deliberations.

MR WEICKHARDT: Yes. I guess there is a risk in trying to raise too many questions, having not seen the whole report, but there is somewhat to me surprising issues that seem to arise. Table 1, for example, which you quote on page 13, seems to suggest that the ACPs - who, I think, roughly over that five-year period will have received about a billion dollars in ACIS grants - have produced about $630 million of additional investment in return for the billion dollars of government assistance. That wouldn't, at first sight, seem to be a wonderful return on the government's investment.

MR BANKS: Can I just ask there: is that a correct interpretation? That's on table 1. I think Philip's adding up 291 and 343 in that third column.

MR McKELLAR: Look, I think at this stage in that table we've simply reported the results as we see them. We haven't tried to interpret them for the purposes of this submission, so we would have to go back and clarify that for you. I guess one of the results that does stand out there is the impact that it's had in terms of production for the ACP components. Certainly in my analysis or reading of the study, we haven't focused so much on the ACP side of things and that may be a question that FAPM are better placed to deal with but, when you look at the aggregate figures there through the scheme, it would certainly suggest that it has, in some way, underwritten or supported their competitiveness, at least in terms of the production results that they are getting.

So it may be assisting in providing support to their securing of contracts or the maintenance of their competitive position rather than being the raw investment numbers that are reported there, but that's something I think one would have to look further into the responses that came from the study to determine what that is implying.

MR WEICKHARDT: Yes. The chart below that suggesting a 170,000 unit decline in production of MPVs in the period of time if ACIS were not there again struck me as a very large number, and this is in a regime where tariffs are not changed, where one would assume, unless this is predicated upon one of the manufacturers disappearing; that most manufacturers would be motivated to try and at least maximise their cash position; that they would be producing over that period of time as much as they possibly could.

MR McKELLAR: Philip, I guess, just in quick response to that, this is a case of reporting the results. The question in effect was, "What would your production have been in the absence of having ACIS and knowing that tariffs were in fact declining to 10 per cent?" That's obviously a fairly substantial impact and I think that one can draw one's own conclusions as to what it means about the potential viability or otherwise of a number of manufacturers in the Australian market in the absence of having an ongoing support for investment, and the transitional support and so on there, to get the investment in place to secure the industry's future. I guess that was one of the key objectives of the program, so whether that says that there's an indication that it may have been successful in at least securing that objective in the near term, I think we have to again read it at face value and people can make up their own minds as to what that is really saying.

MR WEICKHARDT: Yes. It's a much bigger decline than the modelling would suggest, and again you've got the caveats on. I don't know how predictive of real life that would be, but it's a very very large decline.

MR BANKS: A question I was going to ask was on page 18, where you're responding to our options on ACIS, and you say that:

> Consideration must be given to the circumstances in which ACIS would be extended for a longer period beyond 2010.

As you know, we envisaged under different scenarios that it could conceivably go to 2015 with some trade-off in terms of the profile of it. You say:

> The chamber contends this should be done on the basis of an agreed formula.

Would you care to elaborate on that, or is that something that you would provide more detail on in a follow-up submission?

MR STURROCK: We do believe that the future structure of ACIS does need to be more closely identified as the decisions are made by government and as the next stage is advanced in terms of what are the components and how it is established for the future period. We are basically saying that we are not specifically identifying what we believe to be the most appropriate option in relation to your suggestions. We are saying that we have an open mind as to a couple of those issues. Fundamentally, however, we do believe that the renewal of ACIS at the quantum level that has been identified in our presentation is essential and we are saying that, beyond the confirmation of that, the specific issues within it would be things that would be further negotiated and arranged with government.

MR BANKS: Okay. To me, it looked a little bit like you were raising the quantum issue again there, that you were concerned that the profile that we had adopted was that it was contingent on the same quantum in present value terms and that you didn't think that that was appropriate.

MR McKELLAR: Yes. We are still, I guess, contemplating how we finalise our position on that issue in the submission. But I think, with regard to that section, the key issue that we've sought to address is your suggestion in terms of option 1 as to the funding envelope being somewhere between 2 billion and 2.8 billion for a scheme over five years to 2010, and I guess what we've tried to present in our position in relation to that is that we see, in terms of that calculation, really two components. One is, "What are the capped elements of ACIS?" and really that's what originally was interpreted to be the ACIS scheme, capped at $2 billion.

Looking at what would happen in terms of future changes in production and investment and research and development in the industry, we have identified that the demand for credits of a renewed scheme over the period 2006 to 2010 would be every bit as, if not more, pronounced than it is currently. The industry already faces a degree of uncertainty in terms of the impact to modulation in the current scheme. That would be just as pronounced in a renewed scheme, so the pressure in terms of the effective assistance that ACIS provides would be just as pronounced as it is currently. In those circumstances, what we have said is that it is our minimum position. The capped elements of the scheme should be renewed at at least the $2 billion level.

We have said that what was the duty-free allowance - the government's decision in 1997 was of course that that would be ongoing. Through simply administrative reasons, it was wrapped into the ACIS legislation and delivered in that way. The government's decision in 97 was that it would be a continuing feature. We believe that should be dealt with as a completely separate issue. It should remain ongoing and it should remain uncapped. So we haven't expressed in this submission a view about what the appropriate value of that is, or otherwise. It should be ongoing, it should be separate and it should be uncapped.

MR BANKS: Is that predicated on a 10 per cent tariff, though?

MR McKELLAR: Yes.

MR WEICKHARDT: Forget the quantum and let's just talk about the bit that's capped. I won't go into what is and isn't capped, but if there was a quantum of money available, whatever it is, under ACIS, you don't comment as to whether or not from the industry's point of view, if the NPV of that was identical, having it delivered over a five-year period or a 10-year period has any advantages to the industry. I think some people have suggested that having it sooner is better. That's great if you're in the period from 2005 to 2010. After 2010, some would argue that for investment after that period of time, if all the money has gone it doesn't help the industry then adjust. Have you got any comment as to what the chamber's preference really is?

MR STURROCK: We have not fixed a view as to the two alternatives as you have just described. We still have an open mind as to the position. We are wishing to come to a view in the foreseeable future. We are undertaking a number of modelling studies with the companies to determine the most suitable plan of the two, if they were the two options being considered. So at this point in time we haven't got a firm view but we are very cognisant of the impacts that the two may provide.

MR BANKS: Can I just get you to comment. Under Other Design Issues on page 20, you talk about, in the initial submission:

> Consideration be given to ways of enhancing support for innovation.

You then go on to say that:

> This, among other issues, should be determined in consultation between the industry and the government once in-principle decisions have been

taken on the quantum.

Could I get you to elaborate on what you imagine those discussions or negotiations would be focused on?

MR STURROCK: Certainly. I think, like last time at a similar inquiry, having determined the in-principle decisions of policy to do with tariff, this type of investment incentive for ACIS, as it's now called, and other matters, that that is the first stage of the process with government and it's our expectation that this time around a similar process will occur. Having done that, having achieved that and having identified those key policy issues, it is then probable that there would be a period of time during which the government and the industry will work closely together to determine the finer details of those structures.

We have in these comments today and we have in our submission previously in May identified some suggestions as to some refinement to the ACIS structure and referred there to R and D and innovation as potentially taking a slightly higher profile within that structure. They are the sorts of things that would be determined, in our view, as that second-stage negotiation with government. Rather than identify and be specific about those at this point, we see the primary task being to determine the in-principle policy decisions in the first instance and then to enable further work to be carried out at a later time, albeit soon thereafter, to determine the other matters as described.

MR BANKS: Could I put to you though that often the devil is in the detail and the way in which a given quantum of money is targeted can make a huge difference - if nothing else - to the distribution of benefits among potential recipients. Some of your members have raised with us the question of focusing more strongly on R and D, but others have argued against that.

MR STURROCK: Yes.

MR BANKS: How do you resolve those kinds of issues in having an FCAI position that you're putting to the government about the detail of it that you can't actually put to this review?

MR STURROCK: I think the issue is a very fair question, in the sense that there have been quite a number of discussions about those issues already. It's been a matter of consideration also in the Automotive Council meetings and there are inevitably slightly differing points of view amongst the various players, given their particular circumstances. In any event, however, those discussions are very useful and productive and it's important for those discussions within the industry players to be had, but we don't see at this point in time a need to describe precisely what those arrangements would be other than to make the very clear observation that, if the industry is in a strategic sense looking for the R and D innovation as the opportunity to take it further into the world stage, then these matters need to be given potentially a slightly higher profile than may have been in the original scheme.

So that has been the process of our discussion. That's our thinking. At some future point, there will be the need for further analysis to be determined. We would expect that that would be something that would be negotiated specifically with government through the minister at a future time and we're suggesting that probably that time is after the in-principle decisions have been determined.

MR BANKS: Okay.

MR WEICKHARDT: Peter, in your submission, if I read it correctly, when you talk about separate funding pools, you talk a lot about the method of allocation. You don't, unless I'm misreading this, explicitly say anywhere that you are in favour of separate funding pools, but it's implicit in what you say. Have I read that correctly?

MR STURROCK: Yes. We do believe that it would be potentially suitable and that there should be separate funding pools so that it can be more, I suppose, precisely determined for the two major sectors; on the one hand, the motor vehicle producers and, on the other hand, the others - the others primarily being the component producers - and that is our desire and we have confirmed that and we note your suggestion that there perhaps should be separate funding pools. We would support that concept in principle, yes.

MR BANKS: I was going to move onto industrial relations. You've got a very brief treatment of industrial relations issues there. I'm including this as a thorny one, in terms of actual concrete suggestions, and that's the sort of nub of it in a way as to how to take it forward. Could I get you perhaps to respond - and it might probably be easier for you to respond than individual members - to the proposition that we've had put to us as we've gone around the industry. Some have seen that the way in which the assemblers have dealt with their workforces and, in particular, the wage increase that they've provided has constrained or flowed on to them in a way which they felt was unhelpful and placed them in quite a difficult position.

Could I just get you to respond on how your members see the way forward in terms of negotiations with their workforces and, in particular, this issue of, in a sense, setting precedents that make it very difficult for, say, component suppliers to do anything else, so you're constraining what they can do.

MR STURROCK: The industrial relations issue is certainly a difficult one and one we acknowledge will continue to require a good deal of careful management.

Having said that, the just-in-time processes - the efficiencies that have been created in manufacturing right around the world, including in Australia - are things that rely very much on very careful scheduling and a close time frame and very precise just-in-time sequencing.

It is obviously also an issue that we have corporations of varying sizes - from the very large vehicle manufacturers to some of the quite small component manufacturers - and size and scale, management expertise, financial support, financial strength, et cetera, of course vary in proportion to those companies. There can't be a one size fits all in industrial relations and we have, as an industry, maintained our support of the enterprise bargaining arrangements whereby individual workforces negotiate their arrangements as to their own specific and unique circumstances, with flexibilities in others, as it relates to their business.

There should not be an industry-wide circumstance and we do not favour industry-wide bargaining-type arrangements, pattern bargaining or issues that are similar to that. We fundamentally are very supportive of the enterprise bargaining arrangements. We acknowledge that, in so doing, that has certain tensions and difficulties because, on a particular given date, negotiations need to be undertaken and satisfactorily completed and we recognise the workplace has the right at certain times to take action if they believe that progress is not to their liking.

Having said that though, we also acknowledge that, in terms of Australia's internationally competitive position, the efficiency of production, the reliability of supply and our timeliness to deliver product to our overseas customers is today essential and will be going forward just as essential and critical if we are to maintain the growth of our business and if we are to maintain Australia's manufacturing position within the industry. It is an extremely tough challenge.

We have said to various people in recent times that we are most supportive of the government's legislation in terms of endeavouring to secure further reform, as has been placed in legislation before the senate. We recognise very clearly that there has been frustration in the passage of that legislation. We also recognise that the government is endeavouring to secure some movement of the legislation in individual pieces, with perhaps negotiations with the minor parties or with the opposition. The process there is one of some difficulty, we note, but nonetheless we also support the government's aim to endeavour to secure that process of legislation.

We have experienced a number of strikes in recent months which have cost the industry dearly and have disrupted production, both domestic and export, and have again raised the question about Australia's suitability and effectiveness as a supplier. That is regrettable, but I think it's also important to note that all players in the community understand the risks that are attached to those disruptions. We have sought, with negotiations with unions and with other members of the community, a deeper understanding of the growth expectations of our industry, the opportunities which remain and, if you like, the long-term benefits that can be derived through industry growth, stability of production and efficiency, and generation of higher volumes and higher wealth.

I think it's also important to note that we have, by and large, in the vast majority of our workplaces, quite harmonious, practical and realistic arrangements, and this issue of industrial concern or unrest is by no means typical of the wide majority of our industry players. It is, once again, a handful of areas and a handful of circumstances which cause the difficulty and which create the headlines and the media attention, and that is regrettable because it is very important to note that, due to quite productive and constructive relationships with our workforces, we have been able to substantially improve our quality, substantially improve our efficiency, and deliver on the growth, both domestically and export-wise, that is so essential for the industry, and there are some quite outstanding achievements amongst the industry players in that respect.

So again, I go back to my earlier comment: one size doesn't fit all. We have varying sizes of organisations with varying levels of expertise, with structure, with resource, and with capacity to deal with these issues. We are determined as an industry to, as efficiently and as effectively as we can, work through the processes because we recognise that it is going to be essential, if we are to deliver on our growth, if we are to deliver on the long-term strategy, to ensure that manufacturing can remain viable. Nobody in the industry is under any illusions as to the potential seriousness of the issue, if there was to be substantial disruption and if there was to be substantial cost, and so on, as a direct result.

MR BANKS: You say that you are opposed to pattern bargaining but realistically, even within an enterprise bargaining system where you have got common union representation in different workplaces across the industry, there will be an element of that, if not explicit, implicitly coming in. Would you accept that what the assemblers do, what the OEMs do, in a sense sets the stage for what may well happen throughout the industry?

MR STURROCK: Obviously the large corporations may be seen as being a model for other players in the industry, but that is clearly a risk, or an issue. We don't suggest for one moment that that necessarily sets the benchmark or establishes the criteria for other companies and, therefore, if resolution X is achieved in company A, that companies B, C, D and E thereafter think that resolution X should be for them, because again we have got quite differing circumstances and flexibility issues, and other matters which need to be taken into account.

I come back to the first point, and that is that we have, in the vast majority of the organisations, very realistic and practical and productive relationships with our workforces. We have very committed workforces. We have skill levels and so on which are being further enhanced over time and we have, I think, a lot to be very proud of, but that doesn't prevent a handful of issues from disrupting the circumstances and causing what I would describe as a degree of short-term havoc, and that is both costly and very disruptive and, of course, from time to time can receive the sort of unfortunate media attention that doesn't do us any good.

MR WEICKHARDT: Peter, it was put to us during some of our preliminary meetings that, whilst the motor vehicle producers may have a record that is pretty favourable in terms of limiting industrial disputation or stoppage, they have been encouraged, motivated, forced - I'm not sure what the right word is - to make settlements of wage outcomes that are unsustainable, that are not directly offset by productivity benefits and, worse than that, that those then immediately flow down into the rest of the industry, which is more labour intensive in the component manufacturers. But as soon as the component manufacturers attempt to push back at those settlements they get leant upon by the MVPs to settle and get on and not disrupt the industry. How do you believe the industry can break out of that sort of cycle, if you believe that is a real risk?

MR STURROCK: I think we need to acknowledge that the industry has internationally been in a cost-down direction for some years. There is a drive to further reduce costs in manufacturing and that, through the processes of manufacturing, has been occurring. We have seen the direct result of that where products large and small have frequently been produced at prices less expensive than the product previously, and the cost-down process is very important in the efficiency of the industry and, if you like, taking product to market at an affordable price.

I repeat: that has been a trend established throughout the world, and we have been part of that same process. It is driven by the manufacturing processes in themselves, it is driven by technology, it's driven by the IT support to the production efficiencies, and they are the key issues. The industry is committed to continue to maintain that process. There has been elsewhere, as we have seen, rationalisation of platforms, rationalisation of production facilities, and the adoption of technologies within vehicle groups or component groups, in a rationalisation format which enables the costs to be amortised over a wider spectrum. That same process will inevitably continue. It is inextricably linked to the success of the industry going forward.

Now, having said all of that, the commercial arrangements between vehicle manufacturers and component suppliers are, in themselves, quite specific, quite rigorous, and inevitably quite tough, but you would expect that that would be the case, given the cost-down process, given the drive for efficiency, given the way the industry has rationalised, and given the way that we need to continually strive for further cost improvements going forward. I don't think that one can ignore the fact that that would put commercial pressures on those negotiations. Again, in terms of size and scale, the bigger guys potentially have more muscle than the smaller guys; it is simply a fact of life. I don't think we need to necessarily apologise or explain that that isn't necessarily appropriate. It is no different in other industries in the world. Automotive, I would suggest, is not unique in that circumstance.

Nevertheless, I think we acknowledge very clearly that the process of cost-down, cost pressure, seeking further improvement, is a tough business and the suppliers to the manufacturers are clearly having to further improve their own efficiencies, their productive ways, their processes, in order to deliver those cost benefits. Now, in that circumstance of course, the labour relationships, the bargaining arrangements, the deals that are struck with the workforces, have an integral part in the cost process; clearly, there is a pressure there. That is clearly acknowledged, but I don't think we can, or anyone can, contemplate a one size fits all for that. I think we just need to note that that is the industry structure, that is potentially the way it's moving forward, and we need to all work as best we can within that structure to deliver upon what's required.

MR BANKS: You would be conscious of views that have been put in relation to whether the firms are trying hard enough, or whether unions or their members have sufficient incentive to achieve outcomes that really do bring about productivity improvements and lower costs. The issue has been raised as to whether ACIS funding indeed should be made contingent upon particular industrial relations outcomes. I would like to give you the opportunity to comment on that proposition.

MR STURROCK: We have said in our submission, and commented elsewhere, publicly, that we do not see that the two should be linked. Quite specifically we see that there needs to be an industrial relations policy process that is undertaken as a specific determination of the industry but that it should not be directly linked to government policy issues, policy settings and the structure of future support and investment encouragement to the industry. Industrial relations is an important element, as we have acknowledged and we have noted, but we don't see that particular progress or developments in that area should be directly linked to the structure of policy settings in terms of the tariff structure, the ACIS support, the trading mechanisms and so on, as we mentioned earlier.

MR BANKS: In saying that you don't see that they should be linked are you saying that you couldn't see that that would be helpful in any way in terms of getting better outcomes, workplace outcomes?

MR STURROCK: I don't believe directly, because they are two separate issues.

There are other issues, as well. We have environmental issues and taxation and other matters which are all important to the industry structure and important to the future policy settings, but we don't see that there can be any justification or wish to link the two things together. The determination of the industry to further improve its industrial relations circumstance - it's good having a table near the band.

We don't see any weakening of the industry's resolve or determination in ensuring we can further advance the industrial relations circumstances and overcome the difficulties, ensure we have productive arrangements and ensure we can minimise disruption through the enterprise bargaining system. That is clearly our immediate objective and we're putting every effort behind that, as the industry collectively and as individual companies. That remains essential and we will do that as part of our development of the strategy and delivering on, if you like, our wishes and our objectives.

MR BANKS: Thank you.

MR WEICKHARDT: Peter, I don't think you make any direct comment about whether the chamber favours the concept of there being a single union in this industry or not. Do you have any views on that issue?

MR STURROCK: Only to this extent, Philip: that we note that within the industry there are a number of unions - and again it varies company to company. I'm aware that some have two or three, others have six or seven, depending on the type of activity they are involved in. We don't see any desire or wish - and we really make no comment about a point of having a single union. I think we need to recognise recent history. We need to recognise the fact that we do have a number of unions of differing types within the workforces of the industry players and those unions need to be addressed by the companies for their own particular needs, as we currently do. We have made no comment about wishing to change that structure, and I don't think it is appropriate for us to make the comment in any event.

MR WEICKHARDT: Can we just move on to a couple of the issues you make about fuel consumption?

MR STURROCK: Certainly.

MR WEICKHARDT: At the end of your report you do suggest that you have some concerns about that and you would like to clarify alternative approaches before assessing their merit. I think one of your members actually suggested that the right solution here was to increase fuel prices. Do you have any comments to make about that?

MR STURROCK: The only comment I would make about fuel consumption and fuel consumption targets would be this: that we have put before government some 18 months ago a proposal for two cooperative targets for national average fuel consumption going forward. At 2010 6.8 litres per 100 kilometres and 2015 6.3 litres per 100 kilometres. They are both extremely difficult targets and involve an enormous stretch in terms of future delivery. The improvements in fuel consumption of the early 90s, mid 90s, were the obvious and low-hanging fruit improvements that could be achieved, and they have been delivered.

We have reached a point where, in determining as best we can, or forecasting as best we can, the fuel consumption average at the end of the decade, we were very conscious of the independent study which the government commissioned through ACL to determine, at arm's length, what they believe to be the best target that could be achieved by the industry, taking a whole series of criteria into consideration, and they came up with a figure of 6.7 as at 2010. Our position, as I have just mentioned, was 6.8 at that same year date.

The government have in their minds a calculation, which is 6.3. We have put to the government that that is, we think, impossible to achieve as we look forward to future fuel qualities, the improvements in lower sulfur, high-octane petrol, and taking into account the market structure in Australia as compared with market structures in other parts of the world. The matter is before government. We have reminded the government and the minister recently that we need to finalise the matter. We are prepared so to do, but we don't believe that it is going to be realistic to be considering a figure that is better than the offer we have made of 6.8 at 2010.

Having said that, also it is important to note that the achievement of improved fuel consumption, as well as improved emissions to provide a better environment, if you wish, for Australia, is very largely dependent upon delivery of cleaner fuels in accordance with Euro 234 schedules, be they petrol or diesel; secondly, and complementary, the adoption of technologies and engines to enable those cleaner fuels to be utilised and for the improvements in both consumption and emission to be achieved. It is therefore, if you like, a two-way partnership between the two sections of the industry.

We have committed to the improved targets. We have before us technologies and engines, both for locally produced vehicles and imported products that can deliver on those improvements. We are wanting to ensure that we can schedule the introduction of those technologies, albeit at considerably higher costs in our vehicles, but we must do so with the certainty of the delivery of the fuels and the target dates, as described, so we are keen to ensure that the negotiation with government can be completed, hopefully, in the next couple of months, so we can lock those issues away firmly.

MR BANKS: Unless you have any other points which you would like to raise I think we have detained you long enough. I would like to thank you for attending today and being first cab off the rank. I think we have had a very useful discussion and we look forward to seeing the submission that elaborates a bit more on some of these points coming to us by 2 August - I think that is the date. Thank you again.

MR STURROCK: Thank you very much.

MR BANKS: We'll now break for five or 10 minutes. Thank you.

MR BANKS: Our next participant is the Federation of Automotive Products Manufacturers. Welcome to the hearings. Can I ask you please, sir, to give your name and position.

MR UPTON: Peter Upton, chief executive.

MR BANKS: Good. Thanks for attending the hearings, again, for coming to this first stage of the hearings here in Adelaide. Thank you also for a pretty extensive first submission that you've provided, which was quite useful to us. I understand you have some verbal comments you want to make at this stage anyway on our position paper and we will take it from there in terms of further discussion.

MR UPTON: Thank you, Gary. Once again, good morning everybody and thank you, Gary and Philip, for the opportunity just to comment on the commission's position paper through this hearing process. I have mentioned to Gary that I may well take the opportunity to put a brief supplementary further submission as an outcome of today's proceedings. Let me begin by saying that FAPM welcomes the commission's preliminary findings. We see them as a very positive contribution to the debate about the future of the Australian automotive sector. As we indicated in our initial submission to the commission, the automotive component sector sees the next 10 years very much as a decade of opportunity.

We expect exports to grow as new markets open up, increasingly complex technology will favour Australia's skill base, and consumer demand for differentiated vehicles will suit flexible manufacturing. Over this period, however, we also expect some substantial changes in the way cars are built, in the structure of the world automotive industry, in the competitive pressures on suppliers, both locally and overseas, and in the form in which components and systems are delivered to the vehicle assemblers. While the industry has made considerable strides over the last five years in improving its efficiency, there is still some way to go, particularly in the areas of R and D and capital investment. That is why the component sector regards ACIS as critical to the industry's future.

The key findings in the commission's paper, which are most welcome to us, are that there is a shared optimism about the industry's future, there are benefits in having a long-term policy plan for this industry and the term of decade of policy certainty with a continuation of ACIS as its cornerstone has been put forward. The economic efficiency gains from further substantial tariff reductions are small and the industry requires sufficient time to make the necessary changes to secure its long-term viability. In this statement I now propose to concentrate on our comments on the main post-2005 assistance options canvassed by the commission. Rather than getting into specifics about the pros and cons of each of those options, our comments will be directed more towards expressing the general principles and directions we see appropriate.

First, the tariff rate: The tariff remains, in our view, an effective policy element for multinational companies in winning automotive investment into Australia against competing locations. Principally for this reason FAPM's position - and I'd say in this regard it strongly mirrors our colleagues from the federal chamber - is that the long-term general tariff rate for automotive products should be held at 10 per cent post-2005. If and when APEC takes effect in 2010, the specific concessional rate for APEC member countries could perhaps be set lower than 10 per cent, consistent with our international obligations and, in response to reciprocal tariff cuts in other member countries, the non-APEC rate might remain at 10 per cent.

We believe that the case for further unilateral tariff reductions is now not compelling. Usually the argument has been that it has been in Australia's national interests to act unilaterally, as the principal beneficiary of efficiency and resource allocation gains has been Australia itself. However, the modelling undertaken in the course of this review suggests that the gains to Australia from further tariff reductions are at best small and may indeed not be forthcoming. We would say it is therefore arguably consistent with our national interest to continue the tariff at 10 per cent until this changes or at least, as we have suggested, until there is real progress on the market access and trade liberalisation fronts as have already been extensively covered this morning. It's in this context that the tariff is important. It has a symbolic significance, we would argue, as a demonstration of government commitment to the automotive sector, and it's in this context too that I think it can be seen as a bargaining coin in the process of securing better market access.

Extension of ACIS: The extension of ACIS beyond 2005 will have a substantial positive effect on the confidence of the Australian industry to secure the necessary investment and R and D funds for longer-term viability. Such an extension has the strong support of the component sector. We polled this at our recent convention and I have to say that the support was unanimous. Tariff levels and the structure of ACIS are also closely interrelated. As the commission has noted, the relative impacts of the three ACIS approaches will depend on the quantum of funding attaching to each and the basis on which that funding is to be distributed to firms - page 124.

FAPM is reluctant, therefore, to push forcefully for any of the particular options outlined by the commission at this stage. However, some general comments we feel we can make on the current ACIS design which are relevant to any future arrangements for the component sector include incentives tied to R and D and capital investment which have worked well for the component sector and we believe they are well targeted. Notwithstanding the industry successes to date, there is still some catching up to do. On this point I'd simply note that, as the commission says, parts of the industry are still some way from being internationally competitive; hence, the abrupt withdrawal of ACIS in combination with a renewed round of tariff reductions could be sufficient to precipitate the exit of firms that might otherwise have become internationally competitive under a more accommodating arrangement - page 123.

This catching up: industry believes that this is the critical decade it has in which to do this and lessening the benefits of ACIS reduces the industry's ability to attract the investments which will underpin change. We therefore endorse the commission's comment that there are sound reasons to retain the scheme substantially as it is and modulation has, nonetheless, caused some uncertainty, and a funding level better tied to expected claims might be beneficial. Capping and separate funding pools: for physical management reasons it is understandable why the commission would support the capping of more credits. However, uncapped credits are not available to component producers and so the FAPM is not taking a position on this matter.

In our original submission, we stated that FAPM is opposed to any suggestion that ACIS effectively be split into four separate schemes by partitioning the funding for each category within the total ACIS budget. Under the present ACIS provisions all firms within the automotive industry have to compete for the limited capped funding. Only MVPs have access to uncapped funding under ACIS. Those non-MVPs undertaking the highest levels of plant and equipment investment and R and D spending receive a higher share of the available funds, as it should be in a competitive market. Non-MVPs have also to compete for that funding with MVPs who receive most of their credits based on the value of the vehicles they produce.

Around 75 per cent of that value is made up from the value of components and other services supplied by non-MVP participants in the scheme. If partitioning were to be favoured by the government, FAPM would suggest that the amounts available to each participating group should be based on a sound economic rationale such as relative contribution to industry value added, rather than on some historical assistance allocation unrelated to economic efficiency. If it were decided to change the basis of earning credits for MVPs more towards R and D and P and E expenditure, then we believe that separate funding pools become relatively imperative to prevent the MVPs from draining the common pool.

This was implicit in our statement on page 78 that FAPM would not oppose enhanced support for MVP plant and equipment and R and D expenditure provided it was not at the expense of other participants. Any enhanced support in these areas must be financed within the fiscal cap by commensurately reducing either the uncapped or the capped production credits available to MVPs. If the government did decide to create separate funding pools - and this is a variation on the position put in our original submission; simply that we hadn't thought of that particular method - FAPM would tend to support the commission's suggested method of financing those pools on the basis of relative unmodulated claims on the total expenditure over 2001 to 2005.

Other comments: most of the other findings by the commission are broader in nature. While the federation generally supports the direction of those findings, we think it unlikely that much progress will be made in going down what are already some quite well-travelled roads. For example, the manufacturing industry continues to complain about the 3 per cent revenue tax imposed under the tariff concession system and has done so to no avail since it was introduced. Calls for general reviews of Australia's R and D system and its workers compensation system are supported, but at the moment they do not appear to be supported by government. As the commission is aware, workplace arrangements and industrial relations issues have become very prominent. These are important issues. FAPM is an active participant in the process of trying to secure the best possible outcomes in this process for all participants and will continue to engage in productive discussions with those participants.

In summary, let me reiterate: we believe that the commission's position paper provides a sensible and constructive blueprint of the future of the automotive industry. Thank you.

MR BANKS: Good, thank you very much for that. With the slight distraction of the noise, we might have to come to the IR points that you were making towards the end there, Peter. Could I just go back to some of the comments you make in relation to the tariff. I think in your initial submission you may have had an even harder line on the tariff, in the sense that I think you were saying that we shouldn't do anything on the tariff until all developed countries have bound their tariffs at zero, which might have been stronger than what you are suggesting now. But just so I can understand, you're saying that the way you see APEC would be us making potentially an APEC-specific rate a contingent on what other APEC countries did, and then leaving the tariff at 10 per cent - in other words, having a kind of discriminatory tariff, depending on whether a country was in APEC or not. Is that what you're proposing?

MR UPTON: In effect, yes.

MR BANKS: The APEC commitment, as I understand it, is what they are calling concerted unilateralisation or unilateralism, in that countries have made a commitment to reduce their tariffs or their protection which is not explicitly reciprocal in a sense like in the WTO but also is MFN based, so that under APEC it wouldn't be discriminatory either. So in that sense it's not a formal free-trade area or anything like that. In a sense you are saying that we should scrap APEC and start again.

MR UPTON: I'm not sure that I'm saying that. I think what I am saying is that if there was a genuine move to free within APEC, the logical position would be that we would retain a tariff towards others who weren't in APEC, and at that point that would become a bargaining counter with them; in other words, it's a powerful inducement to move everybody to a rate of free if the countries that are within APEC quite genuinely all move to free trade.

MR BANKS: I don't want to get tied up in the technicalities of it, but I think there would be WTO problems with that. I mean, APEC was explicitly reconstituted as a free-trade area under article 24 or whatever of the general agreement. So, in a sense, I'm not sure that what you're suggesting there is operational, but it might be something that, if you wanted to get back to us with further thoughts, you could elaborate a little on.

MR UPTON: Yes, okay.

MR BANKS: Does the notion that Australia has had some sort of significant role in relation to APEC and therefore there are demonstration effects from Australia's position cut any ice with you - that proposition - or not?

MR UPTON: I was interested in the discussion you had earlier. I think that Australia's role as a first mover in APEC obviously has to weigh somewhat with government in considering that. I'd raise the question as to whether or not saying that, for example, we will continue the tariff at 10 per cent till 2010 has any implications for that, and I suppose really the crux of the position that we're taking is that there seems no reason to bind ourselves to a particular tariff reduction regime thereafter. That is a subject which could be looked at again perhaps more closer to the time.

MR BANKS: I don't want to get preoccupied with APEC, because it was only one strand of the various things we were looking at, but implicit in that is your judgment that 10 per cent would meet the Bogor requirements.

MR UPTON: Well, I'm not sure what the Bogor requirements mean. There's been a bit of probing around what exactly a commitment to free within APEC means. I suspect that some might have difficulty in accepting that 10 per cent meets it. I'm not saying that, if the general move in APEC is to come to fruition, we should not do what we've said we'd do. I'm taking the point that's been made by others that we shouldn't continue to be unilateral about that. I accept the nicety of the argument that says we were the leader in the pack and therefore we've got some obligation to not be seen to renege on our commitment. I'm simply saying that I don't see a continuation of the tariff of 10 per cent till 2010 and no commitment to do anything in particular with it thereafter is reneging on that commitment.

MR BANKS: Okay. You talked in your introductory remarks about the tariff - that the tariff was critical in winning investment - and certainly I think we got an automotive industry in this country because of the tariff and it's well known that multinationals sort of relocate behind tariff walls. How critical do you think 5 percentage points of the tariff are to winning international investment? How large do those 5 percentage points loom, in your judgment, against all the other factors that will determine profitability?

MR UPTON: I think that's a fair question. In and of itself, I suspect the answer is not great - that movements in the exchange rate are likely to be as significant on a day-to-day basis. That's why I'd use the term "has a symbolic significance". It is an indication of the government's attitude towards support for the automotive sector. Movements in the exchange rate have no such symbolic value. They may be more real, but the fact is that they come and go, as evidenced in the last few weeks. There's been a movement one way followed by a movement the other way. That's not atypical, but the broad world does not read any particular significance into those sorts of movements - they just happen - whereas, when the government takes a firm and definite to position to say, "We are unequivocally committed to reducing the tariff by a further 5 per cent or to reducing the tariff to zero," say, then that clearly has a symbolic significance.

I can't place a value on it. I think essentially those sorts of estimations are going to be subjective, but I think the existence of a government commitment to the automotive industry has a quite significant effect in terms of people who are considering Australia as an investment location. It's the change in that rather than the direct consequence of it, and yet that doesn't say that it may not be, at a point in time, significant. Clearly, if you were to reduce the tariff to a point where ACIS was also reduced and the exchange rate was moving against you, then you've combined a triple whammy. So it might at a point in time achieve a particular significance whereas, if you took the assumption that everything else remained the same, it might of itself not be particularly significant.

MR BANKS: This is something on which I guess we'll continue to talk. Even on a symbolic level, I think the direction of industry assistance in this country is reasonably clear and protection policy would have been reasonably clear over time, and yet we've seen significant investment in the industry. So it's a bit hard to see, from past experience, that foreign investment has been so sensitive to the tariff phase-down or reduction program. I guess you're saying that, once the tariff gets lower, it looms larger in significance. It's hard for me to be convinced by that.

MR UPTON: Yes. It's an argument on which it's possible to have different views, I'd say.

MR BANKS: That's true.

MR WEICKHARDT: Peter, a number of people who made submissions to the inquiry made the point that volumes among some manufacturers in Australia - and I don't think they are necessarily thinking only of component manufacturers, but let's confine it to that for the moment - are still way below those that might be seen to be internationally competitive and they therefore suggested that significant further industry rationalisation would be necessary. Is that an issue that you have a position on? Do you agree with that? How do you believe the government should best help facilitate that in a sensible and helpful manner?

MR UPTON: That's a good question. I think there's a general consensus that the process of rationalisation that's going on globally has further to run in Australia. In some cases that's quite probably related to the volume of production that's being done in Australia and the limitations on the ability to expand that. I'm not able to comment in detail on any particular firm's case, but I expect there is more rationalisation in the industry to come, and the point about how that rationalisation can be managed from the government's point of view is one I haven't given a great deal of thought to.

MR BANKS: Okay. If I could just ask a couple of questions about what you said on ACIS: you talked about ACIS being closely related to the tariff. We've also talked in those terms. I guess we've had quite a strong view in the position paper that ACIS indeed is a transitional vehicle that's related to tariff reductions and I'd ask you to elaborate a little bit on how you see the rationale for ACIS in those terms.

MR UPTON: I'd simply repeat the feeling of the federation's members that ACIS is the critical support mechanism at this point in time for the industry. I think that the flavour of the comments I've been making is that we see the relationship as postulating between the tariff and ACIS for the moment, and they're clearly linked in the calculation formulas for the way in which credits are derived. So that linkage is more or less inevitable. I suppose one of the thrusts of the argument I was making about tariff is that at some point you might want to review the linkage between tariff and ACIS - in other words, it shouldn't be seen as inevitable that those two things should be coupled in perpetuity.

I accept that that's the government's view or has been the government's view - that ACIS is a transitional assistance measure designed to ease the industry's transit to a lower assistance regime, a lower tariff regime - and certainly, speaking for the federation, we accept that that is an end point; that at some point the industry has to compete on its own merits at the same level more or less as every other manufacturing entity in Australia.

MR BANKS: So what would you imagine would be the longest period in which you could justify a transitional instrument of this kind?

MR UPTON: I think that's going to be a question that is going to have to be looked at again from time to time. Circumstances do change, and you might find that you project a nice straight line to some end point, but something changes and you would need to have a look at that, and the framework within which the commission is proposing looking at it - out to 2015 - seems reasonable to us.

MR WEICKHARDT: I might be doing you an injustice, but I think your original submission suggested that the government really ought to have some sort of review mechanism around ACIS on an ongoing basis that had the opportunity of adjusting, finetuning the way the scheme worked. I guess I struggle with the concept of that against the sort of desire of the industry for certainty and predictability. I know it's early days in ACIS itself but, in terms of providing people with some certainty with long investment times, can you talk a bit about the sort of concept you have in mind?

MR UPTON: Yes. I think you're referring to the comments we made earlier about the potential for having some sort of ACIS impact-monitoring and measurement of key performance indicators. This arose from the observation, when we started to think about our experience with ACIS, that the scheme was operating without any particular defined key performance indicators and arose from some thinking we were trying to do to say, "Well, how would you actually measure the effect of it?" One of the outcomes of that was the work that Deloittes did on the ACIS effectiveness study, which has been discussed already this morning. We, I suppose, advanced that as an idea to say that if you were trying to justify some particular level of funding for ACIS mark 2, it would be useful to know what you got for ACIS mark 1 and, once again, I would refer to that study as being a work that arose from the same sorts of considerations.

MR BANKS: Again, in your original submission you were arguing that the future development plan of ACIS should be, in a sense, developed in consultation with the industry.

MR UPTON: Yes.

MR BANKS: In the light of our position paper, I'm just wondering whether you have any refinements of that view. I think initially you were arguing that that included the quantum of ACIS. FCAI has talked about really establishing the quantum out of this review, I guess, and then going on to the detail design being the subject for negotiation. But do you have a view that has evolved since the original submission on this matter?

MR UPTON: I think our view is that, in consultation with FCAI, we think it's important to settle the details of the quantum of the assistance, but we would add to that the view that we think the present scheme should be left largely unchanged, so inevitably there will be a period of consultation about some details, I would imagine, but we think that the position is that the present scheme ought to roll forward.

MR BANKS: Okay.

MR WEICKHARDT: From that point of view, are you agnostic about whether or not the motor vehicle producer scheme is changed to have more of a bias towards R and D? Do you have a view on that?

MR UPTON: We have put a view already in our principal submission that we wouldn't oppose that, but that immediately raises the question of the design of the scheme, I think, in the sense that, if you reward R and D on exactly the same basis, then it is indeed one pool. In a sense, at the present moment ACIS is two pools, because ACPs and the others earn a credit under ACIS in a quite different way to the MVPs and, if you change that, then quite clearly it has implications for the pool. It is for that reason that we have moved to a position of supporting separate funding pools.

MR BANKS: When that noise erupted outside you were talking about FAPM's position on some industrial relations issues. I guess it's fair to say that at least in terms of the recent disruptions in the industry that they have occurred in the component area and we have had the FCAI talk earlier about "just in time" and the vulnerabilities that come with that.

MR UPTON: Yes.

MR BANKS: I apologise for not remembering some of the points you're making but, in the light of that, can I get you to respond as to how you see this being dealt with and, again, as I asked FCAI, whether you see any linkage of ACIS money to the industrial relations outcome as being helpful in this respect.

MR UPTON: I think that wasn't so much the loud noise in the background but the fact that I made very sparse comments about the industrial relations issue. I would like to place on the record that by far and away the greatest bulk of FAPM's members are also members of the Australian Industry Group, which is the industrial respondent to most of the awards which operate throughout the industry. Disruptions to supply are of very great concern to the industry, and we're obviously closely involved in trying to secure better outcomes from the industrial system.

Nevertheless, that said, we support also the structure of the enterprise bargaining arrangements that go on because that provides the possibility of genuinely negotiating the sorts of outcomes that are required at the firm level to deal with the differing circumstances you face in the industry. But in accepting an enterprise bargaining framework you also accept the possibility of serial disruption - as somebody has termed the phrase - in the sense that it means that every enterprise bargaining agreement has to be negotiated, as its name implies, enterprise by enterprise, rather than a "one size fits all".

Dealing with the fact that we have unions which overarch the lot, there is obviously an issue about how you can avoid flow-ons from one award to another. I would say apropos of EBAs negotiated by the OEMs - and there is quite clearly a pattern which emerges, which is that those become "the ask" in successive generations of awards which follow from that, but I suppose it is like the chicken-and-the-egg argument - where is the pace-setting point in there? I don't know the answer to that.

In some degree that is just a comment on the process that the unions adopt in this - the bargaining tactic - and it doesn't necessarily indicate the outcomes you can get because, if I read the Department of Employment and Workplace Relations submission correctly, there was quite a spread in outcomes of EBAs in the component sector; some, quite surprisingly, tough, compared to negotiations that had been made upstream. Nevertheless, I think the supply sector remains very vulnerable and, in some senses, is the meat in the sandwich in that it is obvious to a union contemplating where to strike that you can have a very strong effect against the entire automotive sector very quickly by picking off key suppliers.

It is therefore necessary to put on the record that, no matter how good your industrial relations is, you may still be the victim in the process in that, and there is very little you can do about that. All that being said, the strong focus the FAPM is trying to encourage throughout its membership is that there needs to be a lot of work done in trying to ensure that, as much as possible, management can secure and align the interests of the workforce with those of the firm, which is the object of enterprise bargaining. Enterprise bargaining ultimately aims to get to that.

We think there is a lot of work that needs to be done - the story is still a patchy one in that regard - and it is always very tempting to try and teach your grandmother to suck eggs, but I should say that there are some very exemplary illustrations of those sorts of alignments in the component sector and there are some not so exemplary ones, and the aim would be that we would be trying to work broadly to improve the worker-employer relations, because at the end of the day the experience of a recent round of pattern bargaining efforts was that, if the workers did not support the union's push at a point, it gave a quite different outcome if the management had lost the ear of the employees.

MR BANKS: Yes.

MR UPTON: So it's tough work. It's not going to happen immediately, but that's the direction in which we think it has to go.

MR BANKS: So is it implicit in what you're saying that there's a lot that management needs to do in terms of improving performance?

MR UPTON: Yes. And on the other front, which is taking cognisance of the particular requirements of the industry caused by the just-in-time process - you know, we should put on the record firmly that abandoning the just-in-time process is not an option. That is the world standard and, if anything, it is becoming even more so. To step back from that places cost into the system again and therefore directly a tax competitiveness so that's not really an option. But to take particular account of the just-in-time requirements of the industry, the federation has supported the common action by the FCAI and the AIG, to propose to the heads of political parties a couple of commonsense amendments to the industrial relations door: one to provide for cooling-off periods and the other to provide for the termination by the AIRC of protected industrial action if significant damage is to be done to a third party.

Now, it's sort of fairly hard, looking from underneath it all, to see how an individual FAPM member can much change the outcome there, but to the extent that we can, we will be pushing those sorts of commonsense approaches and working on the other front which I just outlined. To deal with the final issue you raised, no, we don't support linking, in particular industrial relations outcomes with industry assistance, and the reason is because it's very hard to see how that can do justice across the range of circumstances which the industry finds. If such a linkage were to operate immediately, for example, there might be firms who had three years of industrial peace through simply having recently completed their EBA negotiations and that begs the question of how you would in fact link assistance in the first place.

Let me be very clear, we don't favour it and what I'm now saying is some of the reasons why I think we wouldn't favour it is that it could have quite contrary outcomes in the circumstances of particular firms.

MR BANKS: Okay. In terms of the significant management challenge ahead, do you have any views on what practical pressure can be brought to bear to, in a sense, get managers to focus more effectively than they've done on the workplace issues or on the issues that need to be resolved within our own workplaces, because I think in part that's the motivation for this proposition that has been floated to use ACIS as more of a stick than a carrot?

MR UPTON: I think that in the context of what I've been saying, it's education rather than anything else, other than that people have to perceive that that, quite clearly, is a necessary course of action; that improving all that's within your power to improve is of the highest priority. I think that's just an educational task, and I might add there that from that point of view we, with the AIG, have produced quite a range of materials dealing with various industrial issues and various avenues of assistance that are available to firms in that regard.

MR BANKS: Okay.

MR WEICKHARDT: Do you or your members have a position on this concept that was floated by some, that to resolve demarcation issues it would be beneficial to have a single union? Others have pointed out that that's not a utopia either.

MR UPTON: No, the federation doesn't have a position on that. I would say that you'd find members would take different views on that, and we certainly haven't tested the membership on it.

MR BANKS: Just moving around a little bit, if I can perhaps just get you to respond on the question as to whether the local OEMs, the motor vehicle producers, have played a sufficient role in facilitating exports of components to parent markets, if I can use that expression. Have they played a role in that? Is there more scope for that to be developed?

MR UPTON: I think the major role that the local OEMs play is exporting cars and, to the extent that the OEMs export cars, of course, they provide component producers with the easiest export sale of all, and so we're very firmly of the view that what can be done to promote export of motor vehicles from Australia is in our own interests. There may be opportunities, which I'm not aware of, whereby the local OEMs could directly assist their suppliers by, for example, arranging introductions into the supply chain, by being prepared to recommend them, subject of course to the usual quality and so on being met. Those things seem to me to be possibilities, but I'm not able to comment specifically on how well or badly those opportunities have been exploited in the past. We'd certainly like to see them exploited in the future.

MR BANKS: Okay.

MR WEICKHARDT: Just going back to ACIS for a moment - and I know there are a lot of issues around ACIS in terms of the quantum of funding available - but one of the issues we were looking for feedback on, that I think you didn't comment on, was the pros and cons of delivery of more money over a shorter period of time or a lesser quantum over a longer period of time if the net present values of the two were identical at the starting point. Do you have a view on that?

MR UPTON: I can report that the solid view of the membership is that it's the more money over the shorter period of time and that's what underpins the comment that we see this as the decade of opportunity; and we're talking about this decade till 2010.

MR BANKS: All right.

MR WEICKHARDT: Is that option 1 over five years your strong preference then?

MR UPTON: That's right.

MR BANKS: Okay.

MR WEICKHARDT: The other thing I was going to ask you about is, some people have commented on the AMADS scheme and other people have not. I guess we were left a little uncertain as to how strongly the industry really believed this was something that was essential or the degree to which they really ought to be doing this sort of thing - the sort of market development work themselves anyway.

MR UPTON: The origins of the AMAD scheme, one of the larger pieces of which was to fund the access concept cars, I think lay at a point in time when the Australian industry was not well known abroad and was seen as a focusing endeavour for promoting the entire industry on a world stage. I think the decision was taken after the industry in effect ratified the decision after the second concept car that that method of promoting the industry was no longer required; that did not mean that there was no promotional effort required for the industry but that something different needed to be done.

So we would like to revisit that issue with the government or certainly to express the view that something is required to be done, more targeted, more focused, recognising the different market circumstances that prevail now.

MR WEICKHARDT: Graham Spurling, in his submission, commented on the fact that there should be more pressure on the OEM manufacturers to look at commonalisation of parts, that this was one of the things that was inhibiting the competitiveness of the industry - it didn't give component manufacturers the volume that their international peers might see in larger markets, and there seemed to be a nodding of head that this in theory is a good thing but in practice it just doesn't seem to have happened very much. Do you have any views on that?

MR UPTON: I missed the opening point. Was it you said that Graham had said that the - - -

MR WEICKHARDT: This commonalisation of components that the OEM should agree on - you know, say a single design of shock absorber or something like that - to give the component manufacturers better economies of scale.

MR UPTON: Yes. The only thing I can say in relation to that is we have that under discussion with the OEMs at the moment through a forum that we share with the FCAI. We, at the component sector level, regard it as an issue predominantly for the OEMs. While it may make sound sense at least as a theoretical proposition, the means of effecting it are well beyond the component sector, I think. I suppose we're amongst the nodders who say, "Yes, that in principle might be a good thing to follow up but let's see what happens."

MR BANKS: I think one of the virtues or advantages of you not providing another submission is that it makes for a briefer conversation.

MR UPTON: Yes.

MR BANKS: But, certainly, we would appreciate if there are any things that come out of this, or any elaboration of your views on paper would be helpful to us. Again, we've got a fairly tight time frame on that but we will leave it to you to think what you can do there. Any other comments you want to make?

MR UPTON: No, I think that's it from me. Thank you very much for the time.

MR BANKS: Good. Thank you.

MR BANKS: Our next participant is Air International Group Ltd. Welcome to the hearings. Could you please give your name and your position for the company?

MR GRIFFITHS: Yes, Bruce Griffiths, managing director of Air International Group.

MR BANKS: Thank you for attending the hearings today and for the submission and indeed for the earlier submission, which was very useful and we may even have a couple of questions on that earlier submission but, as discussed, give you an opportunity to summarise the main points you want to make.

MR GRIFFITHS: Thanks, Gary. I guess just as an introduction, just to explain who we are: Air International is a little different inasmuch as we are an Australian-owned component producer. We've moved from a small-bit player to a substantial player in the industry, and therefore some of the problems that we face and some of the issues we face in respect of the industry and its settings are probably - we are a microcosm, in our view, of what the industry faces, I think.

From our perspective the commission's documentation provided so far - we commend the commission on the work done and the options put forward and the arguments that support those options. So we're very encouraged by the position that you put and believe that it's a good document from which we can build and flesh out some specific other views. In broad terms, our organisation very strongly supports the FAPM submission. We are all part of the component sector, and the component sector has a broadly common position across most of its elements, some unique elements, which we would talk to as we go forward.

On the issue of tariff, our position is consistent with that that's been spoken to today by both the FAPM and FCAI inasmuch as we agree that the tariff should broadly be paused at 10 per cent till 2010; that although the commission recommends that the tariff should then be reduced to 5 per cent, either in a step or progressively to 2015, your own report comments through the modelling that the assistance that the tariff provides in regard to economic benefit is marginal, at best, and I refer you to your own document at page 165. It broadly says that the economic gains are generally very small. Given those uncertainties, we wonder why perhaps, beyond the 10 per cent position, we should lower tariffs at all.

We've certainly put the position that we have, as a country in the region, led by example on the tariff position. We have not seen market access become available to us. We have not seen reciprocal commitments from others and, therefore, we don't believe that leadership should continue blindly forward until we can start to see some gains through market access and leverage. If we were to choose an option out of the option papers that you put before us, it would be 3, which was the step down of

1 per cent per annum. We would prefer not to do that without a further review along the lines of that stated before benchmark: the performance of our near neighbours.

On the scenario of ACIS, specifically, it's clear from an industry-wide perspective it's been a successful formula. From our company's specific position, it's been spectacularly successful, and I will talk to that a little further at little later. I think as a benefit to an Australian company with Australian investments, trying to make its way in the world, it has had a powerful impact. We have made massive investments in our organisation over the period of ACIS which could not have been done had the ACIS scheme not been available to us, and our organisation is substantially more diversified than it was prior across a broader spectrum of products and, in the process, has taken some actions to rationalise some of the component sectors - elements of the seat business.

There's a range of activities that we've taken, and I think we've only just started on that course. I am sure that that rationalisation will create, not just by our organisation but by others who participate in the component sector, economies of scale, higher volume and the opportunities for standardisation which, in itself, gives more competitive pricing. When we look forward at the next five to eight years, pretty much the vehicle platforms that we are producing products for are replaced by our customers and therefore we actually face substantial further investment in the short term. I guess when it comes to the assessment of the options that you have put within your paper, we are strongly of the view that the ACIS quantum needs to be made available to the industry through this transitional phase in the first five years of that cycle - in the 2005-2010 period. So we would strongly agree with option 1.

We understand, and there's been some discussion this morning - and we've actually been a participant in the agreement - that ACIS is a transitional scheme. What we've got evidence of, however, both in our own firm and in the work done by Deloittes, is that the return on investment in our view of that scheme is very substantial indeed. The comments made earlier, or your questions, Philip, earlier of the general submission made by Deloittes, which I don't think you've seen yet but commented to in the FCAI document, we feel when you take that data generally, it does become, to some extent, a blancmange and needs to be discounted because of enthusiasm. We've taken a view that you may be somewhat sceptical about that and, at an enterprise level, in our own organisation been fairly rigorous about assessing the value that ACIS has been to us and our investment decisions. I'll talk to that in a moment. I think that we recognise your suggestion is that the ACIS scheme perhaps shouldn't be tinkered with; that perhaps it should roll on in its conventional sense.

We are talking about something in the order of three or three and a half billion dollars over the next eight years, and it's important, in our view, that it is correctly spent. We make some comments in our detailed submission but, broadly, it's worth a good look to make sure that it is going in the right direction; that if there is some finetuning, it should be considered because of the quantum and because there may be enhancements to the return on investment that in fact the taxpayer can get from its use. I don't think now is the forum. We may even come back to you with some ideas just to expand on some of the issues that were made in our last submission.

Coming back to the specifics of ACIS for our company, and without getting into the micro-detail, our organisation in the period of ACIS till now has moved from about a 250 or 280 million dollar business to a 550 million dollar business and next year we'll do 740 million dollars of sales and 860 in the following year on the back of the investment we have made on ACIS. The indirect contribution that we calculate through our work with Deloittes to the economy and the flow-on effects of consumption-induced production we believe to be in the order of 1.1 billion. When we look in the micro, our view is that for every dollar of ACIS money we've received, we've directly spent about $10 in research and development, capital investment, excluding issues of buildings and other things which are not ACIS dependent.

When we project with Deloittes the multiplier effect of that into the economy, the number is $30. It's a very substantial issue, and even discounting those numbers for enthusiasm, and we've been pretty rigorous to try and be able to sustain a position that was seen to be conservative, I think it's a very substantial return on investment. In respect of the market access subject, and it's been briefly discussed earlier this morning, it's a particular problem for an Australian business that's trying to make its way in the world. We are not part of an international division. We have to generate returns in this on our Australian business and reinvest those returns in the development of our market offshore.

The multiplier effect is very difficult because the cost of entry into those markets off an Australian dollar - the marketing costs, although it adds competitiveness in the sales of the product because of the Australian dollar, the costs of marketing are astronomic. To give you a perspective, we have an operation in China with 385 people in it and four ex-pats. The labour cost of those four ex-pats is the same as the 381 Chinese. It's an enormous cost of doing business, and that's an operating cost. At a market development level it's much higher. So we are strongly of the view that the structure of a market development program needs to be integral in the development of our industry strategy.

The 20 million dollars that's been available under the AMRAD scheme I think has been well spent. Most of it has been well spent. The performance of the AMRAD scheme has been strong in terms of market awareness through examples of the US promotion we did in Detroit a couple of years ago - the access vehicles and so on. For a small country and a small market, to make a presence in the world, we have to be innovative about the way we do it, and consistent and continuous, and the fact that that scheme has ceased already - 30 June - and that there is a gap between now and whatever the post-2005 arrangements are is, I think, of major concern. We have also, under that scheme, spent substantial amounts of the $20 million on trying to derive market access with limited, if not no real results yet.

If we give up that process we won't make the gains we need to make so we're making our presence felt but we haven't yet broken through, and our view is that we should be a continuum in that area. I guess my last comments really come back to the issue of industrial relations. We would like to think of our organisation as a leader in industrial relations. However, I've got to tell you that as of yesterday we were put on notice that we will have a strike on Tuesday. So the issue is a hot one in our environment, and one of the issues for us is clearly that the lean manufacturing system, just-in-time and sequence deliverers and the supply industry will continue to be targeted unless we can find some legislative - we support the legislative changes that are proposed - cool-down periods, third-party effect protection, et cetera.

We're very concerned that the vehicle producers would argue that their industrial relations appear to be more robust than that of the component sector. We don't believe that at all. We are strongly of the view that it's purely about finding hot spots in the supply chain that can add whatever leverage. We are affected by the industrial settlements of our customers and the pass-on effects of those are making life more difficult, and so we do, as an industry, need to find some answers. We do not believe that adding a carrot or a stick, in essence, in industrial relations resolution to industry assistance would do us any good at all. We are strongly of the view that the reverse would be the case; that once that becomes a bargaining chip, in fact the pain and suffering we may face in the resolution of this with unions could be even worse.

On the subject of single unions, we've got mixed opinions, and we ourselves at our tier 1 sequence in line supply sites have single unions and have worked hard to facilitate that. At our tier 2 businesses that are suppliers to those sites, we have multiple unions who, in some instances, have a stronger understanding of the particular discipline. So we're not an advocate either way. I think it is horses for courses. We've had recent experience in North America of the power of the automotive single union in the UAW who used their influence to destroy our organisation's success in having won a contract and using their leverage - threatened that if their small supplier - the biggest component producer in the world - was denied their small piece of market that we had taken from them, that they would stop the car industry in North America. I didn't think that Air International was that important but, clearly, we were.

I don't think any of us want to get to that stage where that amount of muscle could possibly be exercised in our industry. So I think caution should be exercised with a single union outcome. They're broadly the issues, from our perspective. In closing, I think we would observe that the position paper of the Productivity Commission, the position of the FCAI and FAPM is fairly consistent. We will continue to debate between the car-makers and the component sector; the pool in respect of the ACIS bucket and I'm used to negotiating with purchasing people within car companies, and I would rather that we had made that determination outside of those bounds.

We're of the view, I think, that the mix of share of the pool today is about right and that its separation needs to be done. There is pressure that does get applied to us continuously to leach those gains that are in fact enabling our company to restructure itself and invest in new technology and to reflect them in today's price. We are resisting, and will continue to resist, that because it will destroy the transition of the industry. So we are strongly of the view that that process needs to desist. I guess that's, in summary, my position.

MR BANKS: Thank you, Bruce. That was a nice summary of the points that you've made and we'll come back through some of those. The first point that occurred to me was your point that - quoting from our own report that we'd said that - in your words - "the gains involved were generally very small". I had a quick look where that was in the report and it's in the modelling appendix. I guess the point I would make in response is that in the chapters, we try to put the modelling in perspective and, clearly, the modelling in terms of staticality of gains and all of that technical stuff does not generate a lot of action, and that's sort of inevitable given the tariff has come down significantly.

In the old days, when the tariff was quite high, that modelling sort of swamped everything else and so the dynamic issues and the adjustment issues really were unlikely to be a significant consideration relative to those, although I should say perhaps in the past they should have been given a bit more consideration than they were sometimes. So we went on then to think about, "Well, what are the other things that you would look at?" and I guess maybe we haven't done it well enough and we need to do more in the final report, but we looked at a range of considerations that aren't picked up in the modelling, either under the general heading of Dynamic or other more qualitative considerations. Some of those had to do with the fact that there is still quite a significant tax on consumers, which is there, and we have the ACA and people from Western Australia berating us for not sufficiently taking account of that.

MR WEICKHARDT: Australian Railways is an organisation.

MR BANKS: Exactly, so we're getting that perspective. So that is just indicative that there is a cost that someone is bearing in that sense. There are also questions of a distortion in the tariff structure itself between four-wheel drives and passenger motor cars, which is less of an issue, I guess, if we're seeing convergence, and I suppose we see convergence down rather than up. I will just finish and we can talk a bit about it. A third thing is the question of APEC, which we don't see as the overwhelming issue but we do see it as an important contextual thing and, indeed, as we've said in the report, certainly a repudiation of APEC could backfire on us, to the extent that if other countries were encouraged to meet their APEC obligations that would bring very significant gains to us, and the modelling does show that, at least when it's across the board.

The last thing that I'll mention now is just this more subtle question of the relationship between assistance and productivity, which is another dynamic thing, and I suppose the concrete manifestation of that is the pressure on the industry, both management and workforce alike, to get their act together and to do better. You've made the point in your earlier submission that there's a limit to which that argument applies. I guess we're not convinced that the argument is finished yet and, indeed, would see a signal to have no further change as perhaps being an unhelpful one in terms of a workplace negotiation context. So they're just a few reactions and, as I say, maybe we need to do more but if your other point is right, that we have at least addressed reasonably well the arguments, then it shouldn't be such a mystery.

MR GRIFFITHS: I guess the point I'd make is that once you've moved tariff from 15 to 10, then what should the rate of tariff be and why is the notional 5 per cent a number? What is free trade? What is the number it needs to be? If we are to take your view that there should be some continuum of the process, then a number of 5 per cent has no relevance to me. I don't understand its driver. What should it be? And I wonder, should we be studying that number before we make that step, that next quantum step.

MR WEICKHARDT: You probably won't like the answer, Bruce.

MR BANKS: I guess there would be people who would say the appropriate number is zero, and we haven't heard from Ross Garnaut yet in this inquiry, but he put a submission into the general tariff one where he argued that - we've had talk about symbolism, that the symbolism of zero tariff is quite useful; it reduces a lot of transaction costs and makes people believe that from now on it's - you know, the notion of government bailing them out, and it's sort of gone forever, so we're in the realm here of more qualitative argument. I guess our approach is to make that as transparent. It's a judgment issue to some extent.

MR GRIFFITHS: I think at the component level or, certainly at our business's level, we would take the view that the tariff is less of an issue for us, as a maker of components, other than it will stop the volume of production of cars in this market and that would destroy our volume on a component competitiveness basis - that is what we make versus what we would be able to. Someone could buy against us as an importer at a lower rate of tariff. I'm not too concerned. What I am particularly concerned about is I need customers on which to build a business base from which I can become international, from which I can create volume, from which I can then add competitiveness to those domestic customers and, if that is denied, then the whole cycle that we're on - and quite uniquely I think for a few of the component industry suppliers and only one or two of the Australian-owned businesses - I think it would be a sad day to see that happen.

We've had a grind into import volumes getting beyond 50 and now closer to 65 per cent of market share. We have moved the industry to a level of competitiveness technically, and from a competence - from an industrial relations, from a logistics management perspective - to a point where we are not there but well on the way to success and we should be able to claw back our market share in vehicle production in this market. We have that as an objective, as the participant in the Automotive Council, as we seek the industry's perspective - a process of setting a vision for 2010 and 2020 for the industry has gone forward and, clearly, getting back to an Australian production volume of 50 per cent plus of the market is something we need to be able to do and we need to be capable of getting there. That critical mass will come.

MR BANKS: I take the points you're making and I guess it's been our judgment in the position paper that the proposal we're putting forward isn't going to jeopardise that and that - I mean, if we're talking about the modelling, for example, the modelling, which tends to be pessimistic in a forecasting sense, shows that that production would be inclined to - there'd still be production growth but it may not be growing as fast as otherwise. In the past, generally productions outperformed what the model would have said anyway and there are limits to modelling can do. We've taken the points you've made but have tried to balance them in the sense of other internal considerations, including the ones I mention plus external ones in APEC.

MR GRIFFITHS: We don't win all our arguments, Gary.

MR BANKS: No, that's right. We've talked about it being a more subtle and complex process and therefore we value that kind of feedback, because on some of those issues there it's a question of judgment being exercised about different parts of it.

MR WEICKHARDT: Bruce, you referred in your introduction and also in your submission to the possibility of getting a sort of better bang for your buck from ACIS by some finetuning. You talk about the fact that maybe it would be worthwhile looking at targeting ACIS on increases and output, and I think by inference you mean by increases also in plant and equipment investment and increases in the increment in R and D.

MR GRIFFITHS: About setting KPIs. Going back to a point raised earlier, that says, "Should ACIS benefits just flow naturally through the system and be consumed as they're spent?" Those that are leveraging their businesses, increasing their investment, going forward with growth, going forward with rationalisation or diversification, perhaps should be rewarded in a different manner. I don't know how to do it. That's an element that we consider is an issue.

MR WEICKHARDT: But can I just clarify - you are talking about increments in all three areas, are you?

MR GRIFFITHS: Yes.

MR WEICKHARDT: Right.

MR GRIFFITHS: And setting some KPIs for that. Maybe the issue then as you approach modulation, the method of modulation is then the tuning fork, as it were.

MR WEICKHARDT: Do you have a method in your mind of avoiding a sort of gaming process? Today, this year, it's sort of Air International increases its production significantly. Next year it's Griffiths Newman Inc that sort of starts a new component manufacturing company that increases its production to - - -

MR GRIFFITHS: You have to set rules. I mean, I haven't considered doing the wrong thing, so I can't conceive of the concept. The other element I think that's unique for us and perhaps a few of the component producers is the differentiation between what's deemed to be R and D under the guidelines of what ACIS qualifies and what's considered to be R. Those companies that are Australian based, who are in the research element of their product cycle have a product cycle that's probably three or four years longer than the development element or the application to the engineering element, and I think it's in our interests as an industry to be encouraging elements of R, not blind R but elements of research and development that could create strategic advantage for us.

The cycle of ACIS, as it has been five years, wouldn't even contemplate a research project and then an application to engineering and getting it to market cycle. So we've been very strongly of the view that we need certainty over a 10-year cycle. We need to understand the hurdle; we need to understand the KPIs for continuance, for the assistance to be available to us and the transitionary steps. But there is very little R done in this country. That that is done is deemed to be high quality. Of the brake companies, Pacific have had some sensational outcomes. There's a range of companies that are doing that and are making gains; they should be encouraged.

MR BANKS: Just a comment: you've got some brief comments here on market access which reiterate some useful material in your earlier submission, Bruce. You talk about the original submission putting up some novel suggestions in terms of access to developing countries, and I can assure you that we did think about those, and we will think about them a bit more. I guess maybe with my background implementations seem to loom pretty large as a problem for something like that. The developing countries have had this special indifferential, as they call it, special indifferential position within the WTO which I've always found unhelpful and actually counterproductive in some ways, so we'll give a bit more thought to that. I guess it led me to think how you see developing country markets in your future, from your company's point of view, relative to developed country markets. Bruce, would you like to comment on that?

MR GRIFFITHS: Yes. The issue of market access has been problematic, and a constraint to our business. We made a decision in 1995 which said that we can't be an exporter and we then became an investor, on the other side of the tariff barrier in the developing world, and we've made investments in Malaysia, Thailand, China - multiple investments in China - and in India. What that has done is actually dragged through research and development, dragged through exports of components, so we have sort of jumped over the tariff barrier regime.

MR BANKS: Then you've imported components from Australia.

MR GRIFFITHS: Yes, some - not much. We're not bringing any product back into the Australian market.

MR BANKS: No.

MR GRIFFITHS: We will, over time, do that but we've got to bring those products and those markets up to global competitive standards, which is very difficult to do. As we're progressing in China, we're making progress towards doing that.

MR BANKS: These are joint ventures, are they?

MR GRIFFITHS: Some are joint ventures, some are wholly-owned subsidiaries.

MR BANKS: Have you been able to get concessional arrangements for the imports that you've subsequently brought into the country?

MR GRIFFITHS: A little; not much. Even being an investor in those markets hasn't been able to break down tariff barriers to any great extent. That has enabled us to get a presence in the market. Now, for us, for example, we're well positioned in China as the WTO allows us to get market access and therefore we would be able to pull through higher volumes of Australian-produced components. That task is difficult and I guess one of the problems for us - and part of why we talk about the incentive or a pool of assistance in respect of the market development side - is that the cost of doing that and the cycles of time are massive and particularly difficult if you're an Australian-derived business. Most of our contemporaries are parts of global companies and therefore are able to do those transactions between their divisions. We don't have that luxury.

MR BANKS: Okay.

MR WEICKHARDT: Bruce, you referred in your earlier submission and also then in this one - this issue of market access to the associate companies or parent companies of MVPs - and you say you're not seeking special favours but you're seeking an even break.

MR GRIFFITHS: Yes.

MR WEICKHARDT: What is it you think the government can do in this regard? What policy settings could be put in place that would help? Do you favour some form of conditionality of ACIS funds on this? How would that be regulated?

MR GRIFFITHS: I'm mindful that that would add a constraint to my customers that they probably wouldn't want to bear. Having said that, I've seen in North America - as we all have - voluntary commitments made by the Japanese in terms of their relationship with the North American market over a couple of decades. It seems clear to me that the vehicle producers in this country are very busy doing what they're doing - and they're lean - and making a buck in that industry at their level is difficult. So their ability to actually work and assist the component sector to find access to their parent companies, to introduce them, leverage them, encourage that process is less than we would like them to deliver in my view.

I would like to think that we could encourage a commitment from the car-makers here to facilitate finding their winners and helping them get market access, on the basis of equal - you know, price quality delivery. The cost to the parent companies of those represented in Australia would be zero, because you'd now have to meet all of those criteria, but the pool and the market access that that would give at a component level could be very powerful indeed.

It takes years to take a company like Air International and for anyone to even know who we are. It costs millions of dollars to walk the hallways of Detroit or Tokyo or Frankfurt to get a presence. There is leverage clearly in the hands of our customers to do that, and to help us do it. I don't think you can legislate to do it. I don't think you can create policy settings to do it. I think we should be able to encourage the industry to find an outcome to do that as a matter of course.

MR BANKS: The next section of your submission relates to industrial relations and you've made some more observations there. I remember in your earlier submission you talked about the Edinburgh Park facility amalgamating three separate operations which were covered by three separate unions under one roof, and you say that with one single union on site:

> Although there was some resistance, the AIRC assisted Air to achieve its objective of having only one union at that Holden facility -

or facility near Holden. Could you just explain a little bit how that process went?

MR GRIFFITHS: First of all, the reason it was important was that the investment we've made on that site - and have made a similar investment on the Ford site at Campbellfield - is a recognition that, over time outsourcing will occur because the component sector should be able to do things better than the car-makers can in regard to some areas of specialty. The car-makers themselves are producing some components as individuals for their own consumption, and therefore their volume of that particular task is only their own consumption, whereas if that's rationalised into the hands of a component supplier or two, the reality is they can get critical mass.

We have achieved an outcome in regard to the seat between Falcon and Commodore that sees a quite different seat clearly in the marketing and comfort and styling, but 60 per cent of the product is standardised. It's not a task that can be facilitated by the car-makers. They have not ever been able to standardise between themselves - even petrol caps - but the reality is that the component sector can do that by its relationships with its customers. So that was the imperative: we wanted to be in a position that got us into a union scenario that enabled us to be able to legitimately outsource from that same union inside the vehicle producer to enable their members in essence to be participants in the assembly of those components, if they were outsources. So that was the reason for the drama.

So we started that dialogue - about the strategic logic with that - with the vehicle division well before we made the investment - as we were planning the investment - and they saw the merit. They saw the long-term strategy for it and were very cooperative in pulling that together. We have other sites that accommodate NUW and AMU and so we were able to trade some of those jobs in that location for additional growth in other locations. Fortunately we have been a business that's added something like 300 jobs over the last 12 or 18 months. So we've had some bargaining power over those negotiations. It would be much more difficult in a shrinking environment.

Success in the industry and growth is a good period to enable rationalisation of supplier community and of the union and workforce industrial relations. I think we're in a very good period. We should in theory be in a very good period to leverage these negotiations to our benefit. It will be much harder when we go to the next part of the cycle, the shrinking side of the cycle.

MR BANKS: That's because you're dealing with Greenfield.

MR GRIFFITHS: Well, not only Greenfield. I think you're dealing with additional jobs, you know, net growth.

MR BANKS: You say that the AIRC assisted Air to achieve its objective. In what respect was that important?

MR GRIFFITHS: Look, it was fairly intangible, I think. I wasn't as close to it as - I can't give you any detail.

MR BANKS: All right. That's fine. You mentioned the vehicle division and so on. I don't know whether you'd care to comment on - you made some comments on whether one or more unions makes for a more productive workplace or whatever - whether you perceive any differences between unions in terms of cooperation and - - -

MR GRIFFITHS: Well, certainly the Automotive Union - the vehicle division - understands the industry. It understands the criticality of meeting ships and delivery and the fragility of the supply chain. Having said that, it's a little more subtle and considered in the use of the power that it has. That's not to say it's less difficult to negotiate settlements, but there is a recognition of the flow-on effects and I think our view is that we've been much more comfortable about the moderate positions of the union with the vehicle division than we have with perhaps others.

MR WEICKHARDT: Can I just go back to this issue of the ACIS pools? I think, by inference, you're supportive of the concept of there being two pools - - -

MR GRIFFITHS: Absolutely.

MR WEICKHARDT: - - - and suggested that you don't really want a sort of conventional arm wrestle about the size of the pools. What principles do you feel the government ought to have in mind in terms of trying to think about the way of allocating those pools?

MR GRIFFITHS: There's been a lot of work done in the formation of ACIS to create what were the business plans of the industry and then, as we've gone down the path a little and the industry has got itself energised - both the vehicle makers, in terms of their directions with exports or otherwise, and the component industry, in terms of their investments and directions with exports or otherwise - the modelling of where it's sort of popped out at 1.1 or 900,000 or 900 million or whatever - that proportion seems to be about right.

Our view of your position of the total pool capped and uncapped being grossed together at 2.8 billion and then split 65:35 - I think was your recommendation - we were comfortable with that, but we can't really comment on the uncapped pool. It's not something that we've got access to. We're very keen that our customers don't get access to our slice, because we are investing it - absolutely investing it - in the future competitiveness of our business, the future technology of our business, the market access issues and the internationalisation and the rationalisation and the growth of our businesses. Without it, we would not be investing in the order that we're investing, and that multiplier effect of 1 by 10 is true for us.

MR BANKS: It was a bit unclear how you described that. That is an actual multiplier? You're saying that it's leveraging that amount of - - -

MR GRIFFITHS: Yes. In our earlier submission you can see the net operating assets of our business and you can just see what we've done. We've understood what ACIS was and used it to create what we needed to create for a strong positioning of our business to be a major player - from a minor player to a major player through that process - and in the process have delivered high-performing product, lower cost and more diversification for our customer. A whole range of issues have come in through the process.

MR BANKS: Thanks, Bruce. Did you have any other comments to make?

MR GRIFFITHS: No. Just, again, thanks for the opportunity.

MR BANKS: All right. Thank you very much. We'll break now for lunch.

(Luncheon adjournment)

MR BANKS: We have got three participants appearing jointly: Australian Tyre Manufacturers Association, Bridgestone Australia Ltd and South Pacific Tyres. Welcome to the hearings. I might just hand over to you to give names and affiliations, please.

MR MACKEY: Yes. My name is Greg Mackey. I am the executive director of the Australian Tyre Manufacturers Association of which there are two members, both represented today. Perhaps, if it's okay with the members, I'll introduce them as I speak. Rob McEniry is president of ATMA and chief executive officer of South Pacific Tyres; Andrew Moffatt is the executive director of finance for Bridgestone Australia Ltd; Kevin Halpin from South Pacific Tyres is manager in industry affairs, customer and corporate relations; Stanley Toh from Bridgestone is marketing manager.

MR BANKS: Good, thank you for attending the hearings. I will perhaps give you the opportunity to make some introductory remarks.

MR MACKEY: Australian Tyre Manufacturers and their output represents about half the market, much along the lines of other automotive products in Australia, but its industry association has a long history and, traditionally, has spoken for the tyre industry, the tyre-manufacturing industry in Australia. We have some issues which are common to all components manufacturers. We have, to an extent, a unique position, because we supply very heavily in the replacement market. Tyres are, of course, very much a commodity, but we have an important role at OE level and work very closely with the vehicle manufacturers here. That joint role creates special tensions for us and perhaps issues which we address from a slightly different angle to other components manufacturers.

In the one-page note I have handed up, there are isolated issues which we see as key issues today in our oral addresses. That is not to say that the other matters which we have addressed in our written submissions are not also significant. Generally we found the position paper a very useful document, and stimulating, and we are very pleased in the way that the issues have been laid out. It has assisted us in focusing our own efforts on presenting our arguments to the commission. In making a joint submission, ATMA and its members have suggested that we would each address you on key issues, or at least issues that we feel are important.

However, the major issues - tariff reconstruction, restructuring and the future of ACIS - are probably issues where you, the commissioners, may wish to ask members individually for their views on the options given and the matters raised in the position paper. So it may be appropriate perhaps to deal with those major issues first, and then we would like to bring to your attention these other matters which we say are also key issues for us as an industry.

MR BANKS: Good, thanks very much, we can do that. Something that perhaps differentiates your submission a little from the others in the industry, including component manufacturers, is that you've argued for a significantly slower reduction in tariffs. I think others have accepted generally that tariffs are coming down to 10 per cent in 2005 and you see that really as only the beginning point for a reduction which would go another 10 years. Perhaps we will give you an opportunity to explain why your industry thinks it's more important than perhaps other members of the component sector to keep tariffs at a high level for longer.

MR MACKEY: That thrust of argument has come primarily from the association, rather than from its individual members. I don't think we're that far apart from the components industry generally in accepting that perhaps the three options you've presented are really the three. That hasn't stopped us from putting forward other suggestions. I suppose the suggestion that maybe there is a fourth option was meant to provoke thought and discussion. We had the experience of tariffs dropping to 15 per cent in the early 90s, before perhaps industry generally did. That was a traumatic time for us, and perhaps the memories have remained with us. So we see sudden tariff drops as a threat based on our own history as a sector, and the sector generally, the component sector generally. That is, perhaps, what has prompted that fourth scenario as a suggestion.

MR BANKS: Yes.

MR MACKEY: One shouldn't be bound by the past. Just because of the events in the early 90s it doesn't mean that we are inevitably expecting the same result in 2005. We are a very very different industry now to what we were 10 years ago. That is not to say that we lack courage to face the realities of 2005, whatever scenario is put before us.

MR McENIRY: Maybe I could just add some thoughts there from our perspective. We probably generally accept, over the longer term, that there may be some further reduction, but it's the transition period that we, in particular, are concerned about. There is no doubt, from empirical evidence of the reductions in the past, that these costs or changes flow on very rapidly to the consumer in terms of price, and the impact on SPT is about $2 million per per cent reduction in the tariff. So it does have quite a significant impact in terms of retained earnings and the ability to reinvest in the future.

I appreciate that part of the reduction is to make it more acceptable to the end user, but with that goes some penalties in (a) the types of products that are then imported, and suitability to the Australian conditions and, secondly, the fragmentation that occurs with a variety if import sources that does not give sufficient economy of scale to support the industry and the consumer in the marketplace. So you actually on the one hand give a benefit, and on the other hand you actually penalise the customer in the way they can be supported. By that I'm talking about things like safety, environmental issues and so on, which we will also cover later.

That's part of it. What I might do is continue on with one of the other issues that I see potentially presenting itself in the marketplace. That, in my opinion, will impact the component supplier industry. It relates primarily to modularisation in the vehicle manufacturing sector and how that will impact on the industry totally. I think there is general acceptance that that's the next major shift in the industry, but there is a significant cost that goes along with that. I think part of the issue there is that as the Australian manufacturers move to be more globally competitive, and to meet the significantly proliferating carpark, they are designing and developing niche derivatives of the volume platform to get economies of scale for the volume platform.

That brings with it differentiation of components, appearance items - whatever they may be - and in our industry then specific tyres to meet those requirements. A good example is, say, moving from a passenger-type vehicle with Ford to an off-road four-wheel drive vehicle, which the whole componentry is very different when it comes to tyres. The volume is not great. It requires a different investment level to do that. The other part of modularisation, however, is that the car manufacturers, in our belief, with limited capital that they have, there will be a push-back upstream to the component manufacturers for increased investment for modularisation, either for the assembly of subassemblies, complete sets or whatever, as they move into modularisation.

With that goes significant investments for new facilities, new equipment, online assembly, effectively with industrial parks and so on. Further, there will be a requirement, as that transitions through, for co-development, engineering development and so on. If I look at it from the tyre manufacturers' point of view, and as cars and vehicles become more sophisticated, the issues such as noise, harshness, vibration and vehicle dynamics, and getting that balance correct not only for domestic markets but for export markets, there is going to need to be a much higher design integration and development between the supply network, particularly in areas like suspension, tyres, et cetera.

That puts a significant impost on the supplier network. What we are arguing I guess, or what we would like to put forward, is that that transition, the degree of modularisation and the speed of modularisation, I would suggest is not necessarily defined by any of the manufacturers, let alone the four of them. So we are going to go through a period of varying degrees and different time frames over what could be a two-vehicle life-cycle period as they come up to that level and the industry comes up to that level.

Therefore we're saying, from our point of view at least - SPT's point of view at least - that the ACIS program will be a very important part of the industry plan going forward and, because there's some uncertainty on the time line and to assist in that transition therefore, the tariffs should remain in place before they're gradually taken down out through to 10. We would also put forward that there will be an opportunity, as some of these things become clearer in the industry and there's a more unified approach to how these issues will be addressed, to refine that post-2005 as well.

They unfortunately are unknowns at this time. There are obvious simple steps to it - for example, tyre and wheel assembly, online synchronisation, et cetera. That involves systems interfaces that the supplier would be required or we, as suppliers for those components, will be required to do. There are four manufacturers. None of the systems are the same. So it's going to be quite messy for a single supplier going to multiple customers on the OE market to be able to facilitate that and quite significant investments that will be required.

I guess, in a nutshell, that's where we're coming from. I don't think the industry, as it goes through this next phase, is clearly enough defined in the automotive manufacturing group itself - the time frame. It has some aspirations and some targets, but I don't think the detail of how that will transpire will happen. As they get into derivatives also, to ensure that those derivatives for success in export markets and domestic markets are viable on lower volumes, there will be a further push-back on suppliers' on-sell price to them.

So the component manufacturers are actually going to go through quite a difficult period in our time. That's not saying they can't manage it, but they need the framework and support to be able to manage it through that period, which we believe is really going to commence relatively soon and probably move through the next two major cycles - model cycles - that the manufacturers will bring out. They start, as you probably know, in about 04 and through to 07 and then there will be a five-year gap before the next one.

So there's going to be quite a lot of push-back onto the manufacturers in terms of design integration, investment in subassembly facilities, et cetera. There is obviously the opportunity for a lot of the component manufacturers to leverage intellectual property from their global owners, but you'll still need on-site investment to be able to facilitate.

One of the issues with ACIS then is also the management of the apportionment of the pool as that transition takes place as well. There will be a much larger grab by the automotive manufacturers for derivative developments and new technologies. There will also be from the component manufacturers, as they have to take more of that burden. So the demand is actually going to probably grow, not shrink, on that support. That will balance out a bit, because there will be an equalisation at some point - that they can't do as many derivatives as they would actually like, because the capital can't spread that thinly - but I think you're probably well aware too that they do have some fairly big aspirations in that area.

We're really saying that, over the next five to 10 years, the industry will go through a fairly significant change. There will be pressures on both sides - from the vehicle manufacturers, to meet global standards in terms of the global cars they want to sell on global markets; we will have the same issues. From SPT's point of view, we've gone through a very major restructuring of our operations, as you're probably well aware. It's been quite a painful exercise. The objective was to bring our facilities and operations up to international and global standards, which we have achieved and will continue to maintain. That will give us the opportunity to increase our high-value export programs into the future to support our operations here.

We will have to keep investing in new technologies that are coming out, such as inflation detection devices, et cetera. Fuel economy pressures and legislative pressures will also impact on tyres, believe it or not; on rolling resistance; new technologies and materials to allow improvements in fuel economy results. So we're going to have to make some significant investments in those areas as well, in terms of product. We expect to do that. That's what the market wants. That's what we'll deliver. If you roll all that up, it becomes quite a big burden.

The other thing is, in terms of the tyre industry, there are very demanding requirements from local manufacturers to meet local conditions for the volume base for these platforms. They are in fact increasing. Imported products do not necessarily meet those requirements and would come at a significantly - quite a difficult development process for the local manufacturers. So we actually play a very important part in supporting how local vehicles perform in this marketplace in our conditions - durability, MVH; all those things that are demanded from us to support the local production - if you can wrap that up in about three words.

MR BANKS: Thank you. You've raised a range of things there. Just on the ACIS issue and what we've proposed, are you reasonably comfortable with - we've obviously envisaged an extension of ACIS beyond 2005.

MR McENIRY: Yes.

MR BANKS: Are you reasonably comfortable with what we've proposed there?

MR McENIRY: I was perhaps suggesting that - this probably won't go down too well - it may in fact, during this transition period, not be a large enough pool.

MR BANKS: So you want more, but not necessarily for a longer period of time? You see that period through to 2010 as encompassing most of these transitions.

MR McENIRY: But it's unknown, because the manufacturers really don't have their time lines or the extent of modularisation. So it's a little unknown.

MR WEICKHARDT: Given the fact that your time is short, I'll cut to the chase to a degree. The ATMA paper at one stage refers to the fact that this is an industry that wishes to remain world competitive. That suggests that you believe you are now world competitive. To an outside observer, if I'm direct, this is an industry that looks to me like it's struggling for profitability and viability. Indeed, your suggestions that you need longer, you need more tariff, you need more ACIS, stories about the industry needing to rationalise further, stories about low profitability and struggling for viability, suggest to me that it's an industry that is struggling. The question is, is this an industry that really quite frankly always is going to struggle with two manufacturers in Australia? It seems that you've got very low volumes - that you might be below subcritical mass already - and is this, from the government's point of view, an industry that it shouldn't be propping up with support until it rationalises itself and gets itself world competitive?

MR McENIRY: In the case of SPT, as I indicated, we have gone through a massive restructuring in the last two years. There is no doubt that prior to that time the company was certainly not globally competitive. I would strongly suggest that in fact it is globally competitive now. I think you should be also aware that the company is now trading profitably. So the actions we've taken to reverse the near-death situation of the company have been very successful. The investments we're making and have been making over the last 12 months in facilities and processes are certainly demonstrating our world competitiveness. In fact, we are currently negotiating or having discussions with our partner on exports to their global markets, because of our current and projected cost structures.

MR WEICKHARDT: Given all that, why do you need longer than the rest of the industry to adjust?

MR McENIRY: Because I think the investment levels that will be required on the component manufacturers is unknown at this time and will be proportionately very high for the investment structure of the individual and group component manufacturers of suppliers. It's more the issue of the extent of the unknown. It's not a fear of the unknown. If you look at the steps that may be required: one simple step is tyre and wheel assembly, the next step is corners, the next step is total cross-member subassemblies, right, if you want to look at that part of the car as modularisation. To establish the facilities, the alliances and the investment required to do that, and to co-develop those elements of the car with the manufacturer themselves, is going to require significant investment, and that push-back will be on the component suppliers, I suggest, more than the vehicle manufacturers. I make the point again: their capital will be spent in derivative development.

MR WEICKHARDT: But if you're already world competitive, they can't force you to do something that you don't want to do, and if you don't want to make that investment in modularisation, I assume you won't make it if there's not a payback associated with it.

MR McENIRY: I'd agree entirely with that. I don't think that's necessarily in the best interests of the automotive manufacturing industry for Australia though. The next step is that the whole industry becomes, again, uncompetitive in going forward. What I'm arguing is that the next major change in the automotive manufacturing industry will occur over the next five to 10 years as a total industry, and as a nation we should be aware of that and what support is required for that.

MR WEICKHARDT: But investing money that is not going to earn a sensible return doesn't seem to be very sensible.

MR McENIRY: No.

MR WEICKHARDT: I guess what I'm struggling with is, if you're competitive now and if the move to modularisation is going to aid efficiency and improve the total industry structure's competitiveness, why shouldn't it make a return on its own merit without requiring special government support?

MR McENIRY: I understand your line of argument. What I'm really trying to say though is that there will be a bow wave effectively required. Over a longer-term period there's an opportunity to get a return. It's an up-front investment that will be required over - a return over a longer period. It's being able to fund that proportionately within the structure that will be difficult for the component industry - so for the long-term health of the industry in total.

MR WEICKHARDT: If you didn't fund it, what would happen?

MR McENIRY: That would be a personal projection and I'm not quite sure whether that - of the industry you're talking about?

MR WEICKHARDT: Yes, the industry.

MR McENIRY: It runs the risk of becoming less competitive on a global environment.

MR WEICKHARDT: To what extent are tyres so totally tradable that your customers are indifferent about that? I mean, if there wasn't a tyre industry in Australia, would your customers shed tears or would they just start importing tyres and be indifferent to it?

MR McENIRY: They would. There would be no option if there was no industry here. The issue then is the suitability of those products for the Australian conditions, and the close linkage that they would be able to establish for co-development for such matters as vehicle dynamics which is pressure on vehicle dynamics - noise, vibration; harshness is increasing by the day, it's not going away. As cars become more sophisticated, so will all the development of components and they become more sophisticated.

MR WEICKHARDT: But I assume if those are seen to be of critical issues in the mind of the industry, you can extract some sort of premium for that service, and that presumably aids your ongoing viability.

MR McENIRY: We would certainly be pushing in that direction. Absolutely.

MR BANKS: Again, while you're still here, you mentioned the painful restructuring exercise that you went through. The whole question of restructuring and, indeed, adjustment over time is a significant issue for us to get our minds around, I suppose, and I don't know whether you would like to, just for a few minutes, talk a little about how that proceeded. To what extent were there redundancies involved? How they were achieved; any knowledge you have about to what extent people become re-employed or whatever? I don't know whether you have any comments in that area.

MR McENIRY: Very sadly through this process we've had to take out about 2200 people through the total organisation, primarily in the facilities.

MR BANKS: Over what period?

MR McENIRY: Two years, from December 2000 when we closed the track plant through in fact to next week with the closure of our Thomastown facility. We were very conscious and aware of our obligations to our employees; they received full entitlement. We worked with the government and local communities for other employment opportunities, as did we offer them financial advice service in our placement services during that period. I can't report accurately, I must say, today on the take-up or how successful those out-placement services were more recently with the plants, but certainly in the first plant it was about a 60 per cent - somewhere around there - take-up. That plant was in the same area as the plant next week goes down. I'm not quite sure whether the opportunities will be there to that degree going forward. I'm more than happy to provide the exact numbers to you.

MR BANKS: That would be quite useful, I think - any information you have of that kind.

MR McENIRY: Kevin is just reminding me the issue on the volumes from the plants that are remaining with SBT, and remembering we also have a plant in New Zealand. I'm a bit embarrassed, I guess, to talk about those because it shows you perhaps the sins of the past in SBT, but the unit volume that we will manufacture - and I'm not talking rabbit tonnage because we were doing truck and tractor tyres - is about 90 to 95 per cent in two plants as it was out of five plants. That simply is a reflection, I guess, on poor direction and poor strategic planning previously. We have addressed all those problems at significant cost and earmarked investment for the future.

MR WEICKHARDT: How does that volume compare with that in your parent group affiliates? I mean, take out Swahililand or Botswana, but sophisticated markets around the world. What does the volume look like in that plant now compared to that in other sophisticated international groups in your overall world network? Is it still a tiddler, is what I suppose I'm trying to get at? Is it still a baby?

MR McENIRY: If you look at the North American market, yes. If you look at German markets or European markets, it's probably around half the size. If you look at the Asian markets, where Goodyear, being one of the owners, has facilities, we'd be significantly larger.

MR WEICKHARDT: But those are probably very protected markets, are they?

MR McENIRY: Yes, and they're growth markets because of a whole host of conditions, as you know, that we have to compete with.

MR WEICKHARDT: So about half the size of a European market?

MR McENIRY: Yes. In the global manufacturing footprint, though, for Goodyear this is viewed as a significant player in their global footprint.

MR BANKS: I didn't have any more questions on the remarks that you made earlier. Were there further observations on tariff or ACIS issues that perhaps we haven't picked up that anyone would like to raise?

MR McENIRY: I think I've covered that. I think both of them need to be in play as this next major change takes effect and I accept as a manufacturer that we have an obligation to be globally competitive and able to mix it with the best. We're not concerned about that. We're concerned about the sudden hits and the stability in the industry to be able to work through that.

MR BANKS: In terms of that sudden hit issue - and I think the association talks about 1 percentage point a year declines in preference to sort of step-wise declines over five years - whether you want to give me a perspective from the firm's point of view as to how much comfort that gives; whether you have 5 per cent reductions occurring step-wise over five-year blocks or whether you have 1 per cent a year declines. Is there much in realistic terms? Is there much difference there? In the past the industry has preferred to have a tariff pause and then a more significant decline rather than to see the tariff eroded continuously over the intervening period. If you start at year zero and you're looking at five years, isn't this all factored into the planning anyway, and therefore a higher tariff for longer would be a preferable way to go from a profitability point of view.

MR McENIRY: Yes, I think so. From our perspective, at least, there's not much difference. The step-down simply gives you a better opportunity in that uncertain period that I've talked about. The fact also is though that the changes we've had relative to the changes that are coming are much higher, much greater. So from that point of view the step-down further out is equally - can be managed. I shouldn't say "equally". It can be managed.

MR WEICKHARDT: I think your co-manufacturer in Australia has suggested that they prefer the ACIS option of the ACIS benefit being spread over 10 years. Do you have a view on that?

MR McENIRY: I would support that.

MR WEICKHARDT: And on ACIS - I think the association have suggested that they don't want the pool split into two components - that one component. Again, do you have a view on that and, if so, why?

MR McENIRY: I think the issue is going to be that, as investment requirements in the component industry increases, how that will be managed.

MR WEICKHARDT: So what does that mean in terms of government's thinking about ACIS and one pool versus two?

MR McENIRY: There's a proportional split now effectively. It is going to be how the pendulum actually swings to assist the component group and what formula or mechanism will be put in place to assist that and that effectively then means separate entitlements or ability for entitlements within the overall pool. By splitting the pools there will still need to be a mechanism for changing the size of those pools anyway.

MR WEICKHARDT: I see. You're saying that if your customers push more of the investment your way then they shouldn't be entitled to the same size of pool?

MR McENIRY: Correct.

MR BANKS: Thank you, and feel free when you need to go.

MR McENIRY: I think we may. My apologies.

MR BANKS: We appreciate very much you coming here from Melbourne today.

MR McENIRY: We have left our cards there and we would certainly enjoy your visit to our facility so you can see what we are doing at any time and get a better understanding of the industry.

MR BANKS: Thank you for that offer.

MR McENIRY: Thank you very much.

MR BANKS: We are in your hands as to how to best proceed.

MR MACKEY: It may be best at this stage if Andrew had the opportunity to comment. He has been patiently waiting for Rob.

MR BANKS: Yes, he has.

MR MACKEY: I am sure Bridgestone have some points of its own to make. To save you repeating the questions I think we can assume Andrew has heard them and he can perhaps attempt to address the issues you have raised.

MR BANKS: Thank you very much. Please do.

MR MOFFATT: Thank you very much for hearing us today - I appreciate that - and if I could cover those points raised on behalf of Bridgestone. From Bridgestone's point of view we are supportive of the APMA and SPT position and Rob has explained, I think, the modularisation issue that is facing us in the future and our thoughts on that. If further reduction in tariff levels is necessary we do, for the reasons outlined in our paper, prefer the Productivity Commission option 3.

I think it is necessary to point out that tyres are a little unusual in that they are really a commodity. Yes, Rob has already pointed out that there are unique characteristics to a tyre for Australian cars, and certainly the tyres that Bridgestone and SPT make are tailored to those cars and we supply all four care manufacturers. However, there is a very large level of imports coming into Australia which has posed a threat to our industry for some years, and we're seeing that level of imports steadily increase.

Our industry is very volume sensitive. We certainly need to maintain volumes through our factories to be able to manufacture efficiently and keep our costs down. Supply to the OE car manufacturers is a part of our manufacture. We also supply a large percentage - a larger percentage - to the replacement market and, in that market, we're also being squeezed on margin, so we put a lot of money into investing in new products, new tyres for the Australian OE car manufacturers.

Some of those cars are exported to the Middle East and the US, South Africa, New Zealand, places like that, and our tyres meet all the requirements of those countries, but we are very sensitive to what happens with imports as we see ever-increasing levels of imports come in. There are very low barriers to entry for anybody to import tyres into this country. It is really quite simple. We also face the issue of parallel imports, which causes our industry a lot of grief.

The investments made in the future here are significant, and Rob has talked about increasing requirements of the OE companies. We do have very strict performance criteria for all of the cars that we have to meet, and that requires new technology that we can source from our parent companies, but the investment in capital here is very significant. We are optimistic about the future of manufacturing in Australia. We are very positive about it. At the moment we believe that we are nearing a position to be globally competitive. It's difficult to export tyres from Australia because of obviously very high freight costs out of the country, but also our nearest trading partners have very high barriers which prevent us exporting to those countries.

Our local manufacture of tyres here is operating at about a break-even situation. As we have reported publicly in the press, Bridgestone is a public company and we have reported that our local manufacture has been under pressure. That is true, and we have taken steps over a few years - we have had some restructuring - in an effort to improve that situation so that we can be profitable manufacturing tyres here. We have seen some improvement, and certainly we anticipate that improvement continuing into the future.

The restructuring that I mentioned occurred in 2000 and was really all based at our Salisbury tyre factory. It was not a very pleasant period for anybody involved and similar pain that Rob has already described. We certainly believe that we would like to keep our factory operating here. We believe that we can operate efficiently in the future and compete against other plants. Our factory compared to other Bridgestone factories throughout the world, we are at the small end of the scale, but our quality levels are unparalleled. We do have very high quality standards here in Australia. We have all the quality, the accreditations, the environmental accreditations, and we operate under those rules.

The rationalisation that could occur in the future: yes, we do see some opportunities with modularisation as Rob has mentioned, and the opportunity to provide tyre wheel assemblies to the OE manufacturers, and maybe into further subassemblies. With regard to ACIS, we would prefer to see a continuation of ACIS, and we are supportive of the Productivity Commission's suggestion there. I would also like to mention a couple of other issues, if I may.

MR BANKS: Please.

MR MOFFATT: Firstly, we commend the Productivity Commission for its suggestions of removal of the 3 per cent duty on raw materials. That has been an impost on our industry on local manufacturing for some time - an unfair impost, we believe - and we commend the recommendation to remove that duty. We also made mention in our submission to the commission about developing country preferences. At the moment developing countries receive certain preferential tariff treatment for imports into Australia. It seems illogical to us as many of these countries have manufacturing bases which are very significant and certainly cause us problems when we have imports coming from countries like Korea and Thailand which certainly have manufacturing bases in excess of Australia. We can't export tyres to those countries because of their protection, but it seems that imports from those countries get concessional treatment when they come into Australia.

That also prejudices investment in Australia as far as a manufacturing base. From a worldwide perspective Bridgestone can invest money in a country like Thailand and then reap the benefits of exporting the tyres from Thailand into Australia, but if they invest the money in Australia, the reverse doesn't apply. So it makes an investment decision sway away from Australia. Why would you spend money here? We would certainly rather see money being spent in Australia and invested in Australia.

The final issue I would like to raise is incidental, but also in our submission we mentioned some labour-related issues with regard to things like payroll tax and workers compensation. We see an opportunity now for these legislations to be standardised across Australia. Particularly now we have Labor governments in all states, you would think there's an opportunity there to get some standardisation going between those. It's just an impost on industry; it's inefficient. We're not saying the legislation is good or bad; it just needs to be made standard across the country. I'd be happy to answer any questions.

MR BANKS: We have probably both got some. At one point you talked about making significant improvements and, on the point of becoming globally competitive, how would you identify the main areas in which you could see your performance improving in terms of enhancing your productivity and profitability?

MR MOFFATT: We're continually investing in capital to improve. We've got the benefit of a technology licensing agreement with Bridgestone Corporation which gives us access to high-grade technology, and Bridgestone is the largest rubber company in the world. And through that technology agreement we get access to the technology that they develop. We see the technological improvements coming through in tyres, advances the whole time. We look at a tyre now and look at a tyre 10 years ago and say, "What's the change?" but there are significant changes that occur in compounding.

We talk about rolling the resistance, we talk about fuel efficiency, different methods of manufacture, and through all of those we can see improvements in tyres, we can see improvements in quality, in the life of a tyre, the safety performance in the environmental impact, and improvements in the manufacturing of a tyre. Different companies have their own equipment to manufacture certain parts of the tyre, and that is continually being improved as well. So there are certainly opportunities there and it just never stops; it's ongoing. Bridgestone is a supplier of tyres to Formula 1 racing and the technological developments that have occurred through that are quite significant, and we see those coming through in compounding technologies and so forth. There's quite a bit of development.

MR BANKS: The other question I was going to ask was in relation to developing country preferences. You say that we didn't make a reference to this issue in the position paper. I think we have. It may not have been where you expected to find it, but we did point out that this was an issue, I think, in relation to Korea. It disappears as an issue when the tariff gets down to 10 per cent but it would remain for the other countries, and we raised it as a question of whether it needed to be looked at. It's hard to imagine it being looked at on an industry-specific basis, but we said that this may be something the government would want to look at as a generic issue because it's relevant to other industries as well.

MR MOFFATT: Yes.

MR BANKS: From your perspective - you've mentioned Korea and I think the other country mentioned was Thailand - are there other countries that pose a particular difficulty in relation to the preferential margin?

MR MOFFATT: Certainly I think Malaysia, China, Indonesia are all countries that spring to mind. And Malaysia in particular, I know, has very very high tariff barriers, and Taiwan, of course.

MR BANKS: Yes.

MR MOFFATT: But all those have very significant manufacturing capacity, and we just see it as no longer relevant. Maybe it was relevant when those preferences first came into being, but we believe that day has passed.

MR BANKS: Having mentioned Thailand, I know the industry has been supportive of a free-trade arrangement with Thailand from the tyre manufacturers' point of view. I don't know how you would view that. Maybe that's a question for the association as well. Is it something that you've thought about or made an input into - the wider industry position?

MR MOFFATT: Certainly we haven't looked at Thailand specifically on its own (indistinct) have to but I wasn't aware of that issue just for Thailand.

MR BANKS: Did you have any comment on that?

MR MACKEY: It may well become an issue. It depends how those negotiations develop of course, and the phasing - the time frames that arise. And certainly if there is a suggestion that abruptly a free-trade zone was created between Australia and Thailand we would have to seriously look at the repercussions both short term - because there are major manufacturing plants, I think - both Goodyear and Bridgestone have major plants with huge capacity in Thailand.

MR BANKS: In Thailand, yes. So you wouldn't see an export opportunity coming out of this; it would be more the import implications.

MR MACKEY: Yes. It depends on what a free-trade agreement actually says. It's the indirect barriers to trade that are always more - or as much of a problem and sometimes more of a problem - that you've certainly touched on in your position paper and they're many and varied. It takes time to penetrate a new market, except, it seems, Australia's market. But certainly I think the experience of both members has been that even when you have got favourable conditions to enter a market, it takes time to develop your particular network and your supply chain, or indeed, even the profile of the particular brands that you're selling. We won't penetrate that market from here overnight, so it will be a particular challenge to us.

MR BANKS: Yes.

MR MACKEY: More from tyres coming in, than from us being able to suddenly export there.

MR BANKS: Yes, okay.

MR WEICKHARDT: I guess I'd just like to pursue the issue I was pursuing with Rob a bit more, just to make sure I've understood this properly. I get slightly confused in this industry because on the one hand you describe the product as being a commodity or a new commodity, and the threat of imports ever increasing and the opportunity for exports, and you talk about the ability to tailor-make products for different dynamic effects or local conditions. If this product is a commodity or a new commodity and you are operating plants that are roughly sort of half the world-scale plant, wouldn't the industry be better off with one plant in Australia - even if it's got two people selling - but one world-scale plant that's got a chance of survival, rather than two baby plants that are continually subviability?

From experience in other industry I've just seen these points of rationalisation be put off, be put off, be put off and industry continuing to plead with government for special support, and yet it just postpones the inevitable day when, if the product is a commodity, eventually unless your costs are world competitive, you just want to survive. If the product is differentiateable and people are prepared to pay a premium for that and you've got all sorts of benefits, then maybe small-scale manufacturing can survive with innovation and differentiation. I'm not trying to plan your industry for you, but I'm just testing the case for whether this is an industry that genuinely - if supported for a period of time - can exist in a truly competitive situation or whether you're just putting off the evil day when it's going to have to wrestle with the fact that it has just not got the scale to be competitive.

MR MOFFATT: Certainly you mentioned product differentiation and yes, there is a product differentiation. Technology in a Bridgestone tyre is different to a Goodyear tyre and we are true competitors and certainly they wouldn't let me walk around their factory, and I wouldn't be thrilled about them walking around ours. Each of us believe our products have their own advantages.

MR WEICKHARDT: Do your customers, though? Are your customers prepared to pay differently for them?

MR MOFFATT: Initially there are two really main areas of customers: the OE customers - supply of tyres to the OE market is very significant because it actually helps in the replacement market. If you've got tyres on a new car there's a reasonable chance that you're going to get the replacement tyre. Certainly when you start talking profitability you don't mention profitability and OE company in the same sentence because the two don't go together. Supplying to the OE market is a strategy to enable us to get replacement volume to make a profit at the end of the day.

When a customer comes to replace his tyres, what makes him buy the Bridgestone or the Goodyear product - if they are a discerning buyer and they say, "That is what I need, that tyre was developed for the handling of my car and I want that handling to continue" - sure, they'll buy it. But if they say, "How much does it cost?" they will probably go out and they'll buy a Chinese tyre or a Korean tyre or whatever it is, to put on their car. So that is a problem for us in that there are a lot of products flowing in from many many countries which are very very cheap and coming from developing nations with very low tariff barriers, and they are very cheap to buy.

In that respect the tyre does become a commodity. It becomes a price-driven commodity, because many times you look in the paper and you don't see anybody talking about the merits of tread pattern or tyre compounds; they all talk about the price. From that point of view, yes, it does become a commodity. Certainly the petrolheads amongst us would be aware of the characteristics of tyres and would certainly buy tyres to suit their driving style.

Being competitors, I can't ever see us having a common factory. Maybe that is something for the future but I just can't see it. The worldwide relationship between Goodyear and Bridgestone and other large manufacturers is that we are true competitors in every sense of the word, although we like cooperating to put these suggestions to you. I see there is an opportunity for us in the future. I believe that our volumes here in Australia are sufficient to sustain local manufacturing, but we have to capture the replacement market as well as the OE market and that is why we asked specifically about the developing country preferences; to say, "Well, why should they get a walk-up start in the replacement market?"

We believe that there is some opportunity for export, if we could have a level playing field, but the freight costs make it very very difficult for us. There are some opportunities with the OE companies exporting to countries like the Middle East and South Africa and so forth. Sure, there are export opportunities there.

MR WEICKHARDT: Is the freight impost out worse than the freight impost in?

MR MOFFATT: About the same.

MR WEICKHARDT: So you're getting the benefit in the local market in import parity presumably.

MR MOFFATT: The markets that we're exporting to are not the same markets that the tyres are coming in from. So it's pretty cheap to get from Indonesia to here, but not so cheap to get from Australia to the Middle East. Yes, we are at a disadvantage there.

MR TOH: It's like what Andrew mentioned, and in support of what Andrew mentioned there is that - and I think both of you realise - in order for us to survive we need economies of scale benefits, and that's why we keep on pursuing OE business, because it helps with the economies of scale of our factory. However, if you look at it from a global point of view, what is not available to us is some export markets where the exports from those countries into Australia have relatively low barriers, but we don't have an opportunity to export to those countries. If the playing field was level, then at least we do have an opportunity to exploit further economies of scale, making our plant here truly globally competitive.

Another point that we would like to also make is that with regards to our reaction to tariffs in the future, we are slightly different from other component manufacturers for vehicles in the sense that if you look, for example, at a headlight assembly, or if you look at even the sun visors, for example, those components are specific to those vehicles. So once they have actually got the contract, then the susceptibility to competitors are relatively slim, compared to tyres. Tyres are different and quite unique in the sense that a particular car size that is put on a vehicle can also be imported at any one point in time. It might just have a slightly different tread pattern, but to most consumers they are black and round it goes on the vehicle and it goes around and around.

So I think that from that point of view other component manufacturers might view changes to tariffs slightly differently from tyre manufacturers, because once they've got the contract they are not so susceptible to outside influence whereas, as tyre manufacturers, we are.

MR BANKS: Particularly in the secondary market or the after-sales market.

MR WEICKHARDT: I guess batteries are probably the same.

MR MOFFATT: Just expanding on that point a little bit, Rob talked about the number of models and the ranges that are being built now. Many years ago or not so many years ago - it would have been in the last seven or eight years - the number of tyres supplied to the OE manufacturers was very low. I mean, different patterns and different construction tyres. We read about, for example, Monaro being developed, we read about a four-wheel drive being developed here by Mitsubishi and potentially Ford and we read about different types of niche vehicles being developed.

Every time one of these niche vehicles is developed, we see different-size tyre ranges coming out and then they might have two or three levels within that car. They might have a base model and a medium and a premium level, all with different size tyres. So we see the range of products that we supply growing and tyres that are generally going on cars these days are getting larger. We're seeing larger diameter, wider, lower profile tyres which have different construction methods and, in order to make those tyres, there's quite a bit of capital investment required to actually manufacture those tyres here. It's not just a matter of buying a machine and building a tyre. You're very welcome at any time - an open invitation - if you wish to come and tour our facility. I'll be more than happy to show you just how complicated it is to make a tyre and see how many bits actually go into it and how hard they are to make.

MR WEICKHARDT: Most manufacturers of differentiated products would salivate at that prospect and say the more fragmentation, the more specialisation the better.

MR MOFFATT: Maybe so, but we also rely on volume. We need that volume, because the capital investment up-front is very high. So we need significant volumes of those tyres to actually make it worthwhile.

MR BANKS: You're not talking about a commodity there. As Philip is suggesting, you're talking about a more differentiated product when you're selling to the OEMs.

MR MOFFATT: Yes.

MR BANKS: Does that then dissipate in the sort of secondary market and there's less focus then on having precisely the profile and quality of the tyre that you had on the original car?

MR MOFFATT: It's the same tyre that goes into the replacement market, but it is a problem because if a new car comes out it could be a couple of years before the replacement market builds up a head of steam. So you may have a lag period between supplying to the OEMs and supplying to the replacement market until people starting wearing out tyres.

MR TOH: Also it doesn't help us in economies of scale, where we have to manufacture different size tyres as opposed to in the past perhaps making the same size tyre in volume.

MR MOFFATT: Also it's important what the OE manufacturers are doing in their differentiation - and we're all for it - but it is capital intensive for us and there are a lot of issues there for us to deal with.

MR BANKS: Does that differentiation give you a bit of natural advantage relative to imports in the OE market?

MR MOFFATT: Not really, because a lot of the tyres that are going on these niche vehicles are more performance tyres. So we're seeing that those performance tyres are readily available and, while they're expensive to make, they can also become a commodity very quickly and we do see prices - unfortunately there isn't such a premium on those tyres as you would imagine. You can imagine the range of tyres that is available in Europe.

MR TOH: In support of what Andrew is saying, whilst we might have to go through significant levels of investment creating a particular tyre for an OE manufacturer and then going through the lengthy process of actually finetuning the product to suit Australian conditions, in the replacement market where the tyre market is that open to imports we find that our other import competitors can just come in and capture a slice of the replacement market just like that, because they happen to manufacture a particular tyre in that same size with relatively lower investment.

MR BANKS: Is parallel importing a problem for you? I think it was mentioned by your colleagues there.

MR MOFFATT: Yes, it is. It's a problem for, I believe, all of the large brands in Australia. Parallel importing is a problem.

MR WEICKHARDT: Sorry, can you just help me understand what you mean by that?

MR MOFFATT: Bridgestone Australia Ltd is the registered owner of the Bridgestone trademark in Australia. Parallel importation occurs where another party will import Bridgestone product from Thailand or Taiwan or somewhere like that and imports those tyres into Australia. There are various underhanded ways of avoiding customs duty which I won't go into, but they are employed I believe. They may flood the market with a particular size of tyre or go out into the market, which impacts on our relationship with our customers.

They can bring tyres in. They might buy a huge volume of a particular tyre in that country, get a very good price because of the volume they buy, bring it into Australia, flood the market and cause us problems; cause us problems in our warehousing, distribution, pricing, our relationship with our customers and warranty issues. We're the Bridgestone owner, so if something goes wrong the tyre comes to us. We have to fix it. Technical issues, technical questions come to us. It's a problem. They just take the cream off the top at the beginning, but they don't have any of the ongoing costs or any of the problems.

MR MACKEY: Just to give you an example, a snow tyre. A tyre developed in, say, Japan - or Europe might be a better example, specifically for road conditions there - and it's not uncommon for drivers to have two sets of tyres, a summer and winter set. It's completely alien to our way of thinking, but if they ski regularly they don't have to change their tyres. Those tyres may become obsolete perhaps or be outmoded. They may be warehoused, say, in Singapore for 10 years. They'll be new, but warehoused because they're obsolete.

An entrepreneur will buy them and import them into Australia. They could be Bridgestone snow tyres - not marketed to consumers as snow tyres, but as tyres. Although there may be subtle markings on the tyre that show that it's a snow tyre, it's a code which only the very knowledgeable would understand. Those tyres would be, I suggest, completely unsuitable to Australian - even winter - driving conditions; certainly high-speed highway conditions. There's a safety issue, because handling and stopping parameters would be totally wrong for that vehicle and that driver would have no idea. The tyres themselves, because they've spent 10 years in a warehouse, could have and may have deteriorated. Some of them would. So there are product liability issues that arise at a cost to local manufacturers.

The tyres are tyres, as far as customers are concerned - quite rightly - and, even if there aren't problems in misdescription for the purposes of payment of tariff, there's certainly a misdescription from the consumer's point of view. That's not an uncommon thing.

MR BANKS: My memory of snow tyres is they make a lot of noise when you drive on them.

MR MACKEY: And people say, "Those noisy Goodyear or Bridgestone tyres, I won't buy them again," and it's a real problem. If they'd bought the genuine tyre made here for our conditions, they'd be quieter than the average, not noisier.

MR WEICKHARDT: Can I raise a question then in relation to the submission from the association about the environmental scheme that you have in place; national waste tyre management strategy? I'm a bit confused as to whether or not you're particularly concerned about this, because you are representing an environmental issue or whether this is something that may have environmental benefits, but also gives you some degree of natural protection for the local industry here.

MR MACKEY: Perhaps if I tell you what I think the issue is, and its relevance to this inquiry. We believe that a manufacturer, as part of its costs in manufacturing and distributing that apply, should factor in some cost for the responsibility of recovering the resource at the end of its life and reusing it. In the case of tyres there will never be, I suggest, true recycling in the classic sense. Unlike, say, with glass or perhaps paper - I don't know about paper - you can't complete the cycle. As I think you've heard earlier, there is so much compounding and complexity in putting together that tyre that you cannot break the bonds if you like, literally, the chemical bonds, let alone disassemble the mix of the material to produce the virgin materials you would need at the quality and standard you would need for remanufacture.

Essentially to discharge, if you like, the responsibility of the tyre manufacturers, as producers, to account to the community for the wastage, we have to create a whole new set of industries that will take up the materials and recycle them into other products. So it's not recycling in the circular sense, but in the linear sense. As I say, we have a responsibility. There is a cost in us achieving that. It's part of the cost of the product really. That's an enormous challenge to the automotive industry. In Europe there is a directive that the automotive industry discharge that responsibility by ensuring that no automotive product is wasted to the tip, but is recycled somehow - plastics, metal, rubber and the like - and there are deadlines by which industry must achieve that. Industry is really perplexed to know how to do that.

No-one in the automotive industry has successfully recycled its product, but there have been some tremendous things done, and when I say that in the same breath I say there have been some tremendous things done to separate the waste streams to plastics and metal. Certainly there is a market. What we say is that this is a productivity issue, it's a manufacturing issue, it's part of the cost of being a manufacturer. Those manufacturers who have the idea that they can and should discharge their responsibility as producers need to have some incentive to do that. It doesn't mean that you're a less-efficient manufacturer, and of course you are prepared to cost in an amount, say a levy for example, a recycling levy, into the cost of your goods, or if you have found a way to use recycled material in the manufacturing process. I don't know about Bridgestone, but I know that for some SPT tyres they can use up to 3 or 4 per cent of recycled rubber in actually manufacturing tyres.

All we are saying is those sort of incentives should be encouraged as part of making our automotive industry more productive. Not every sector of the industry can meet that challenge, because it's a difficult challenge. In the tyre sector we think we have got some ideas for recycling the tyre product, not only back into the virgin product, but also into these tertiary industries that I've mentioned. We would ask you to give some more thought to how that might feature in your report. You see, things that go in your report help us a lot when we go to government, because we can quote you. It may not be central to the big issues, the larger issues you've got to deal with, but a reference to the removal of the 3 per cent tariff concession, if you make it again and again in the commission's reports, we can go and quote chapter and verse to the various ministers and departments that we have to see.

Sometimes you have to see three or four on a particular issue. I don't mean this disrespectfully, but we tend to get bounced between ministers on certain issues. Every department seems to think it's some other department's problem. I'm not saying that to be unfair, because it's really the responsibility of a number of departments. For example, with our waste tyre management issue we are having a meeting in August with Environment Australia. They will chair it, but it also involves Treasury, the Australian Taxation Officer, Australian Customs Service. Fortunately there has been a precedent with waste oil and there is now a very successful recycling scheme for waste oil. Ours is dissimilar, but modelled upon that, but the same interested parties will sit in.

They, further down the track, I think, would be very interested in what the commission has to say about this as being part of making Australian industry more competitive. One thing we hope to achieve out of this is intellectual property in the area of recycling, in tracking waste for example. perhaps built into the componentry of the product a means of tracking waste, that is marketable by our industry overseas.

MR WEICKHARDT: I think we have made a general point in the report that if some of these initiatives are important from an environmental point of view they should be tackled on that basis, but that government shouldn't get confused by seeking to, I guess, implement employment or standards for the objective of propping up an industry and assisting an industry. If it's trying to assist an industry it should do so sort of directly, and if it's trying to protect the environment it should do so directly. If it achieves both objectives simultaneously then so be it, but from the point of view of the tyre thing, it would seem to me, from what you've said and as I understand it, that regardless of the source of the product there should be some costs to eventually the consumer for having the product properly disposed of.

MR MACKEY: And consumers are entitled to know how that cost is being used, I think that's the point. There needs to be transparency, but it's not going to give any advantage to a local manufacturer. It's just that local manufacturers happen to have taken the initiative in this instance. Whatever product enters the market it should equally have to bear the same burden and have the same advantages, if you like. If it sees advantages in using its own patented technology to produce a greener tyre, then financially - it doesn't matter whether it's an importer or a manufacturer, we're certainly not suggesting that this is some sort of barrier to trade in Australia that would have artificial environmental standards. In fact, quite the contrary. We would be at pains to keep the playing field level, to use the trite phrase.

I suppose standards, similarly, shouldn't be seen as a barrier to entry into the market, but they should be based on very solid safety and other environmental grounds. I think that a safer tyre usually has more technology injected into it and probably by a manufacturer who was responsible enough also to have a management program for the waste. So you're going to achieve a lot of things in the one package. That usually means you've got to be pretty efficient and effective to do it. So again, you're probably encouraging a leaner production model, because that's the sort of switched-on manufacturer who is going to take advantage of environmental and safety incentives. I just see them as integrated and I see it as wrong to think of environmental and safety aspects only as a potential burden to industry, or as a potential barrier to trade. I think it's quite the opposite.

MR TOH: I think what Greg has said is that, as manufacturers, we are trying to be responsible for product skills, but there is something that is also related to that. That is the importation of used tyres, whereby we have seen that there are actually huge quantities of used tyres in this country, simply because of the fact that in some countries the cost of disposing of a used tyre is actually quite high, and as a result of our relatively low barriers to such items being imported to Australia some countries are perhaps using Australia as a dumping ground for their used tyres. That matter, I think, should be taken into consideration.

MR MACKEY: That's, I suppose, a competitive issue. What Stanley is saying is, these tyres are taken off vehicles when they are three to four years old. They have got some tread life left, if you like, although one wonders why a tyre would be taken off unless it was damaged or there was some reason to take it off. Instead of being disposed of in Europe or Japan or Korea it is exported here and sold in competition with new tyres and, indeed, with retreaded tyres, which are a perfectly acceptable product. If you like, a near-death tyre, which looks - again, it's the deception of a tyre. It can look perfectly good, but it doesn't perform very well at all. Recently the RACV went out and bought 100 used tyres that were being marketed for reuse and tested them at SPT's facilities. They asked if they could use our facilities. They ran a report on the results, and something like 60 per cent of the tyres were either unroadworthy, they had damage, bulges or they were simply worn, smooth and dangerous, or they were on the verge of that.

In Japan about 100 million tyres a year are discarded; somewhere between 15 and 17 per cent are exported. Japan recycles 100 per cent of its tyres because it exports 17 per cent of its waste. We don't get that many in volume terms here, but we could. What happened in New Zealand some years ago, when tariffs were very dramatically cut, was that there was a sudden influx of used tyres into the market in competition with new tyres and the market share that used passenger tyres enjoyed in New Zealand went from something like 7 per cent to 33 per cent in two years.

The year before last, for the first time, a billion tyres were made in the world - a billion units. There are a lot of tyres out there. I mean, 300,000 used passenger tyres enter Australia every year. It's a small amount, but the reason we keep raising it publicly every time we can is because of that New Zealand experience, where suddenly it becomes something that has an impact on a high-volume sensitive industry like ours. Again, what we're saying is that is something you can touch upon in your report. I know it's not central to your main mandate, but the fact that you've touched on it and flagged it as an issue which you see as of concern means that it helps us when we go elsewhere to argue with the powers that be, so to speak, on issues like this that are important to us as a sector.

MR MOFFATT: Just on that point, that also places warranty issues on us because you can imagine if a Bridgestone tyre that has come in from another country, that has already had a life, comes over here and causes problems, generally the person will go to Bridgestone to get a Bridgestone tyre fixed, and we didn't sell it in the first place, and it was damaged when it came into Australia. So that does cause us problems and expense. So it certainly is an issue for both us and SPT.

MR BANKS: You also refer to the 3 per cent revenue duty. I think you approve of the fact that we've raised this and referred back to the earlier report and asked us to reinforce that. My understanding of it is that the government didn't accept the recommendation that the commission made and that earlier report was set to the general tariff and therefore it was a much better vehicle for making a recommendation on an issue of that kind, which goes across many industries. I guess this report also isn't a recommendation focused report, but anyway, we note the point and we note the support for that and I guess we certainly would draw attention to that earlier recommendation, but to what extent we can highlight it, or put it in lights the way you suggest, I guess is a bit unclear given that the government has already responded effectively to it. But we take your point that our reports can be used in various ways, so thanks for that. I did not have any further questions.

MR WEICKHARDT: Can I just clarify one more point about the DC preferences and I am sorry if I am traversing over old ground. When the tariff goes to 10 per cent I understand that Korea's preference disappears so therefore they won't get any DC preference at 10 per cent tariff. What will the situation be of some of these other countries like Malaysia, Thailand and Indonesia in terms of the tariff they're paying today, and what they will pay, say, when the tariff steps down to 10 per cent?

MR MACKEY: It shouldn't apply across the board. There is some uncertainty. We've had some correspondence with the Department of Industry on this issue because in some of the printed material we've seen there's a suggestion - I think it was a mistaken suggestion - that those importer countries would have another step down to maintain the differential to 5 per cent.

MR WEICKHARDT: They're currently at 10.

MR MACKEY: They're at 10 and have been since the last change in the early 90s. That's what should remain the situation if importers are paying 10 from 2005 onwards. There should be no differential. But it is still three years away - two and a half years away - and that, we say, is still a significant period and our concerns remain certainly relevant to that two and a half year period.

MR WEICKHARDT: But your understanding is that once the tariff goes to 10, that that DC (indistinct) will disappear?

MR MACKEY: Yes, the department has written back and stated that, so that's our present understanding. It perhaps needs to be emphasised that present understandings sometimes change but we certainly again see that a reference in this report to the need for that to remain as part of the certainty argument, if you like - that is one issue that we would like certainty of now, to have the comfort to know that from whatever date 10 per cent becomes the norm, that it truly is the norm for developed - you can't make tyres unless you're a developed country, I suppose, is the argument. We're going to have difficulty - well, there are two types of developing countries and this is already a transition and the group - of which all leading major tyre importers, importing at 10 per cent, are comprised - is that transition group. I think there are six countries left in what is left of the group developing countries and none of them manufacture vehicles, tyres or components.

MR BANKS: Okay. Can we do any other - - -

MR MACKEY: Nothing, I don't think, that we need to raise.

MR BANKS: Thank you. It's been an efficient way to proceed, having three organisations together, and we appreciate your making the effort to attend today. Thank you very much. If you have any further comments you want to make to us on paper, feel free to do that. If you can get them in by 2 August - that's the only proviso - so thanks again for attending today.

I'll just ask for the record if there is anyone else who would like to appear this afternoon, otherwise we resume tomorrow morning at 9 o'clock, thank you.

AT 3.16 PM THE INQUIRY WAS ADJOURNED UNTIL
FRIDAY, 26 JULY 2002

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